87-1552
No.

Supreme Court, U.S.
FILED
MAR 18 1988
JOSEPH F. SPANIOL, JR.
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

PETER STEFANOU,
Petitioner,

v.

NORTH RIVER INSURANCE COMPANY, INC.,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETER J. KAHN
Counsel of Record
TERRENCE O'DONNELL
JOHN D. CLINE
WILLIAMS & CONNOLLY
Hill Building
839 17th Street, N.W.
Washington, D.C. 20006
(202) 331-5000
Attorneys for Petitioner Peter Stefanou

March 18, 1988

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

QUESTIONS PRESENTED

1. May judgment be rendered against a civil defendant solely on the ground that he invoked his Fifth Amendment privilege too broadly in response to the complaint, where (a) it is undisputed that answers to the complaint's key substantive allegations could tend to incriminate the defendant, (b) the court has not determined whether answers to the other allegations in the complaint could tend to incriminate the defendant or constitute a waiver of his Fifth Amendment privilege, (c) the defendant has not acted in bad faith, and (d) the defendant is not permitted to replead?

2. Does a civil defendant's invocation of his Fifth Amendment privilege in response to all of the allegations in the complaint constitute a defective assertion of the privilege that permits judgment to be rendered against him, where it is undisputed that answers to the key substantive allegations in the complaint could tend to incriminate the defendant?

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
TABLE OF AUTHORITIES	iv
OPINIONS BELOW	1
JURISDICTION	2
CONSTITUTIONAL PROVISIONS INVOLVED	2
RULES OF CIVIL PROCEDURE INVOLVED	2
STATEMENT OF THE CASE	2
REASONS FOR GRANTING THE WRIT	5
I. THE COURT OF APPEALS DECIDED AN IMPORTANT QUESTION OF FEDERAL LAW THAT HAS NOT BEEN, BUT SHOULD BE, SETTLED BY THIS COURT	5
II. THE COURT OF APPEALS' DECISION CONFLICTS WITH DECISIONS BY THE SIXTH AND SEVENTH CIRCUITS	9
CONCLUSION	11
APPENDIX	1a
A.	1a
B.	8a
C.	23a
D.	25a
E.	26a
F.	27a
G.	28a
H.	45a

TABLE OF AUTHORITIES

Cases: Page

Baxter v. *Palmigiano*, 425 U.S. 308 (1976) 9
Brinks, Inc. v. *City of New York*, 717 F.2d 700 (2d Cir. 1983) 6
Garner v. *United States*, 424 U.S. 648 (1976) 8
Hoffman v. *United States*, 341 U.S. 479 (1951) 3, 7, 10, 11
In re Folding Carton Antitrust Litigation, 609 F.2d 867 (7th Cir. 1979) 7
In re Master Key Litigation, 507 F.2d 292 (9th Cir. 1974) 7
Maness v. *Meyers*, 419 U.S. 449 (1975) 7
National Acceptance Co. v. *Bathalter*, 705 F.2d 924 (7th Cir. 1983) 9, 10, 11
Pagel, Inc. v. *SEC*, 803 F.2d 942 (8th Cir. 1986) 6, 9
Pillsbury Co. v. *Conboy*, 459 U.S. 248 (1983) 6
Quinn v. *United States*, 349 U.S. 155 (1955) 7
Rogers v. *United States*, 340 U.S. 367 (1951) 6
Rogers v. *Webster*, 776 F.2d 607 (6th Cir. 1985) 6, 7, 8, 9, 10, 11
Rosebud Sioux Tribe v. *A & P Steel, Inc.*, 733 F.2d 509 (8th Cir.), *cert. denied*, 469 U.S. 1072 (1984) 6
Temple v. *Commonwealth*, 75 Va. 892 (1880) 3
United States v. *Grabinski*, 558 F. Supp. 1324 (D. Minn. 1983), *modified*, 727 F.2d 681 (8th Cir. 1984) 8
United States v. *Kordel*, 397 U.S. 1 (1970) 6
United States v. *Malnik*, 489 F.2d 682 (5th Cir.), *cert. denied*, 419 U.S. 826 (1974) 11
United States v. *Moore*, 682 F.2d 853 (9th Cir. 1982) 11
United States v. *Murdock*, 290 U.S. 389 (1933) 8
United States v. *Yurasovich*, 580 F.2d 1212 (3d Cir. 1978) 6

Constitutional Provisions:

U.S. Const. amend. V ..... *passim*

Statutes and Rules:

26 U.S.C. § 7203 8
28 U.S.C. § 1254(1) 2

TABLE OF AUTHORITIES—Continued

	Page
28 U.S.C. § 1332(a)	2
28 U.S.C. § 1332(c)	2
Fed. R. Civ. P. 8(d)	2, 4
Sup. Ct. R. 17.1(a)	9
Other Authorities:	
Heidt, *The Conjurer's Circle—The Fifth Amendment Privilege in Civil Cases*, 91 Yale L.J. 1062 (1982)	7
Wolfson, *Civil Discovery and the Privilege Against Self-Incrimination*, 15 Pac. L.J. 785 (1984)	7

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

No.

PETER STEFANOU,

Petitioner,

v.

NORTH RIVER INSURANCE COMPANY, INC.,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fourth Circuit affirming judgment on the pleadings entered by the United States District Court for the Eastern District of Virginia.

OPINIONS BELOW

The opinion of the court of appeals is reported at 831 F. 2d 484 and is reprinted *infra*, App. 1a-7a.[1] The district court's unreported oral opinion is reprinted *infra*, App. 8a-21a.

---

[1] References herein to "App." are to the Appendix to the Petition. References to "C.A." are to the Joint Appendix filed in the court of appeals.

JURISDICTION

The judgment of the court of appeals was entered on October 16, 1987. App. 26a. A timely petition for rehearing, with a suggestion for rehearing en banc, was denied on December 21, 1987. App. 27a.

The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISIONS INVOLVED

The Fifth Amendment to the United States Constitution provides in pertinent part:

> "No person . . . shall be compelled in any criminal case to be a witness against himself . . . ."

RULES OF CIVIL PROCEDURE INVOLVED

Rule 8(d) of the Federal Rules of Civil Procedure provides in pertinent part:

> "Averments in a pleading to which a responsive pleading is required, other than those as to the amount of damage, are admitted when not denied in the responsive pleading."

STATEMENT OF THE CASE

Respondent North River Insurance Company ("North River") filed suit in October 1986 against a Virginia accounting firm and several of its employees, including Peter Stefanou, seeking rescission of three accountants' professional liability insurance policies.[2] North River contended that the accounting firm had falsely stated on its applications for the policies that it was not aware of

---

[2] Jurisdiction in the district court was founded on diversity of citizenship. 28 U.S.C. § 1332(a), (c). Plaintiff North River is a New Jersey corporation with its principal place of business in Illinois. None of the defendants was a resident of either New Jersey or Illinois at the time suit was filed.

circumstances likely to give rise to a claim against the firm or its members. App. 28a-44a.

North River's complaint rested on the charge, repeated throughout the complaint in various forms, that beginning in 1980 Stefanou had knowingly participated in a massive tax fraud perpetrated by one Edward Markowitz. App. 31a-34a, 40a-41a.[3] In addition to these allegations with obvious potential to incriminate, the complaint contained a number of averments concerning jurisdiction, parties, and other formal matters. On the advice of counsel, Stefanou answered by invoking his privilege against self-incrimination in response to all of the allegations in North River's complaint. App. 45a.

North River moved for judgment on the pleadings against Stefanou. The district court made no attempt to determine whether it was "'*perfectly clear*, from a careful consideration of all the circumstances in the case, that [Stefanou was] mistaken'" in asserting the privilege in response to North River's allegations. *Hoffman* v. *United States*, 341 U.S. 479, 488 (1951) (quoting *Temple* v. *Commonwealth*, 75 Va. 892, 898 (1880)) (emphasis in original). Instead, the court deemed *all* allegations admitted—even those with obvious and undisputed potential to incriminate if answered.[4] The district court denied

---

[3] Several months before the complaint was filed, Stefanou had pleaded guilty in the Southern District of New York to federal tax charges arising out of events occurring in 1983 and 1984. The plea agreement provided (1) that Stefanou would not be prosecuted by the United States Attorney for the Southern District of New York for offenses arising from his involvement with various Markowitz-related entities, and (2) that the Department of Justice would not prosecute him for federal tax violations arising from his involvement with those entities. C.A. 50-53. The plea agreement did not protect Stefanou from prosecution in state court, and it did not protect him against federal prosecution outside the Southern District of New York for non-tax offenses. App. 3a.

[4] The incriminating allegations concerning Stefanou's alleged role in the Markowitz fraud were essential to North River's claim

Stefanou's motion for reconsideration, App. 25a, ignoring his offer to replead if the court would rule as to which of the allegations it considered to be potentially incriminating and which it did not, C.A. 146. The district court made no finding that Stefanou had asserted his privilege in bad faith. No evidence was introduced against Stefanou, and he never admitted any of the allegations in North River's complaint.[5]

The court of appeals affirmed the district court's ruling in a split decision. Citing Fed. R. Civ. P. 8(d), the majority noted that "[t]he failure to deny an allegation in a pleading to which a responsive pleading is required constitutes an admission of that allegation." App. 3a. Although the majority conceded that "when properly invoked, the fifth amendment privilege against self-incrimination . . . can avoid the operation of Rule 8(d)," App. 3a-4a, it asserted that Stefanou's "blanket refusal to respond was not sufficient" to invoke the privilege, App. 5a. Thus, the court of appeals affirmed the district court's conclusion that *all* allegations in the complaint were properly deemed admitted, even those allegations, essential to North River's claim, with obvious potential to incriminate if answered.

In dissent, Judge K.K. Hall found Stefanou's invocation of the privilege sufficient and declared that "both the district court and the majority have ignored settled law in this Circuit." App. 6a.

---

for rescission of the insurance policies, since it was Stefanou's alleged relations with Markowitz that, according to North River, had not been disclosed in the applications for insurance. App. 40a-41a.

[5] North River dismissed the action pursuant to settlement as to all defendants other than Stefanou. App. 2a; C.A. 198. None of these defendants was a party to the appeal, and none is a party in this Court.

REASONS FOR GRANTING THE WRIT

The Court should grant the writ because (1) the court of appeals has wrongly decided an important question of federal law that has not been, but should be, settled by this Court, and (2) the decision of the court of appeals conflicts with decisions by the United States Courts of Appeals for the Sixth and Seventh Circuits on the same matter.

I. THE COURT OF APPEALS DECIDED AN IMPORTANT QUESTION OF FEDERAL LAW THAT HAS NOT BEEN, BUT SHOULD BE, SETTLED BY THIS COURT.

The Fourth Circuit wrongly decided an important question of federal law that has not been, but should be, settled by this Court: Whether judgment may be rendered against a civil defendant on the ground that he invoked his Fifth Amendment privilege too broadly in response to the complaint, where (a) it is undisputed that answers to the complaint's key substantive allegations could tend to incriminate the defendant, (b) the court has not determined whether answers to other allegations in the complaint could tend to incriminate the defendant or constitute a waiver of the privilege, (c) the defendant has not acted in bad faith, and (d) the defendant is not permitted to replead.[6]

---

[6] The court of appeals decided this question in part on the ground that Stefanou had not timely asserted his right to replead before the district court. App. 6a. In fact, as Stefanou pointed out to the court of appeals, he *did* raise the point before the district court; in his motion for reconsideration, Stefanou declared that he "stands ready to amend his Answer, invoking the privilege where the Court deems appropriate and responding where the Court finds (1) that the response could not possibly tend to incriminate him, and (2) that the response would not waive Mr. Stefanou's privilege." C.A. 146. The district court never determined which allegations in North River's complaint could tend to incriminate Stefanou and which could not, and Stefanou was therefore unable to amend his answer

The decision of the court of appeals places civil defendants with potential criminal liability in extraordinary peril. Either they can invoke the Fifth Amendment privilege and risk immediate loss of the case if the privilege is later overruled as having been too broadly asserted (as happened to Stefanou), or they can respond to the complaint's allegations and risk incriminating themselves and waiving the privilege.[7] An incorrect judgment can be costly; Stefanou, for example, has lost millions of dollars in insurance coverage. This choice, with little or no margin for error, imposes an impermissible burden on civil defendants' Fifth Amendment rights. Moreover, the issue is likely to recur often in light of the frequency of related civil and criminal proceedings.[8]

---

without risking incrimination and waiver of the privilege. In light of this clear statement by Stefanou that he would replead if the district court would rule on his invocation of the privilege, the court of appeals' assertion that he did not raise the point in the trial court is inexplicable.

[7] In *Rogers* v. *United States*, 340 U.S. 367, 373 (1951), this Court held that one who testifies as to some incriminating aspects of a matter may not invoke the Fifth Amendment privilege as to other aspects. Thus, if Stefanou had responded to some allegations of the complaint, mistakenly thinking them non-incriminating, he could well have discovered later that he had waived his privilege as to all related allegations. "[G]iven the somewhat indistinct boundaries of the 'waiver' doctrine," Stefanou's broad invocation of the privilege "would seem to have been no more than a prudent assertion of [his] rights." *United States* v. *Yurasovich*, 580 F.2d 1212, 1221 (3d Cir. 1978).

[8] The prevalence of such cases is reflected by the large number of recent appellate decisions addressing issues that arise when the Fifth Amendment privilege is asserted in civil litigation. *See, e.g., Pillsbury Co.* v. *Conboy*, 459 U.S. 248 (1983); *United States* v. *Kordel*, 397 U.S. 1 (1970); *Pagel, Inc.* v. *SEC*, 803 F.2d 942 (8th Cir. 1986); *Rogers* v. *Webster*, 776 F.2d 607 (6th Cir. 1985); *Rosebud Sioux Tribe* v. *A & P Steel, Inc.*, 733 F.2d 509 (8th Cir.), *cert. denied*, 469 U.S. 1072 (1984); *Brinks, Inc.* v. *City of New York*, 717 F.2d 700 (2d Cir. 1983); *National Acceptance Co.* v. *Bathalter*, 705 F.2d 924 (7th Cir. 1983); *In re Folding Carton*

This Court has never addressed the precise question presented here. In other contexts, however, the Court has intimated that a person asserting the Fifth Amendment privilege should receive a preliminary determination as to the propriety of the invocation and an opportunity to respond before being penalized for asserting the privilege. In *Quinn* v. *United States*, 349 U.S. 155 (1955), for example, the Court reversed a conviction for contempt of Congress on the ground that the alleged contemnor, who had asserted the Fifth Amendment, "was never confronted with a clear-cut choice between compliance and non-compliance, between answering the question and risking prosecution for contempt." *Id.* at 166; *cf. Maness* v. *Meyers*, 419 U.S. 449, 461 (1975) (noting that "pre-compliance review [for a witness through contempt and appeal] is particularly appropriate where the Fifth Amendment privilege against self-incrimination is involved") (footnote omitted). And in *Hoffman* v. *United States*, the Court concluded that a grand jury witness

> is not exonerated from answering merely because he declares that in doing so he would incriminate himself—his say-so does not of itself establish the hazard of incrimination. *It is for the court to say whether his silence is justified . . . and to require him to answer if it clearly appears to the court that he is mistaken.*

341 U.S. at 486 (emphasis added) (citations and quotation omitted).[9]

Antitrust Litigation, 609 F.2d 867 (7th Cir. 1979); *In re Master Key Litigation*, 507 F.2d 292 (9th Cir. 1974); Heidt, *The Conjurer's Circle—The Fifth Amendment Privilege in Civil Cases*, 91 Yale L.J. 1062 (1982); Wolfson, *Civil Discovery and the Privilege Against Self-Incrimination*, 15 Pac. L.J. 785 (1984).

[9] In *Rogers* v. *Webster*, 776 F.2d 607 (6th Cir. 1985), where a civil defendant invoked his Fifth Amendment privilege in response to the complaint, the Sixth Circuit declared that "if [the defendant's] assertion of privilege had been overruled, we believe he would have been entitled then to an opportunity to respond to the con-

The Court's decision in *Garner* v. *United States*, 424 U.S. 648 (1976), is also instructive. In *Garner*, the Court concluded that a taxpayer who improperly asserted the Fifth Amendment on his tax return could be prosecuted for willful failure to file a return under 26 U.S.C. § 7203, without a preliminary ruling on the privilege and an opportunity to reconsider. *See id.* at 663-65. But because § 7203 requires proof of willfulness, the Court found that a good-faith but erroneous assertion of the privilege would preclude conviction. *See id.* at 663 n.18; *United States* v. *Murdock*, 290 U.S. 389, 397 (1933).[10]

The requirement that willfulness be proven under § 7203 was the key to the Court's holding in *Garner*. *See* 424 U.S. at 666 (Marshall, J., concurring); *United States* v. *Grabinski*, 558 F. Supp. 1324, 1333 (D. Minn. 1983), *modified on other grounds*, 727 F.2d 681 (8th Cir. 1984). Under the ruling of the Fourth Circuit in this case, by contrast, a civil defendant can have judgment rendered against him without any finding of bad faith or willfulness, without the court determining whether answers to specific allegations could tend to incriminate him or constitute a waiver of the privilege, and without an opportunity to reconsider his assertion of the privilege and respond on the merits.

---

tempt charges of his adversary." *Id.* at 611-12. The court correctly noted that a person asserting the Fifth Amendment privilege in a judicial proceeding "ordinarily 'receives a judicial ruling at that time on the validity of his claim, and he has an opportunity to reconsider it before being [penalized] for refusal to answer.'" *Id.* at 612 (brackets in original) (quoting *Garner* v. *United States*, 424 U.S. 648, 663 (1976)). *Rogers* concluded that "[n]ot affording one who asserts the privilege an opportunity to answer, once his claim of privilege has been rejected, is to penalize him merely for asserting the privilege." 776 F.2d at 612.

[10] Moreover, the Court noted in *Garner* that the taxpayer would usually receive a preliminary ruling on his privilege from the IRS. *See* 424 U.S. at 664 n.19. Thus, the taxpayer ordinarily would have an opportunity to reconsider the privilege before prosecution.

This Court has never decided whether a civil defendant can be penalized in this manner for invoking the Fifth Amendment too broadly. The writ of certiorari should issue so that the Court can resolve this important question.[11]

II. THE COURT OF APPEALS' DECISION CONFLICTS WITH DECISIONS BY THE SIXTH AND SEVENTH CIRCUITS.

The Fourth Circuit's decision conflicts with decisions of the Sixth and Seventh Circuits holding that judgment on the pleadings may not be rendered against a civil defendant solely because he invokes his Fifth Amendment privilege against self-incrimination in response to the complaint. *See Rogers* v. *Webster*, 776 F.2d 607, 611 (6th Cir. 1985); *National Acceptance Co.* v. *Bathalter*, 705 F.2d 924, 932 (7th Cir. 1983).[12]

The court of appeals purported to distinguish *Rogers* and *Bathalter* on the ground that "[n]either case dealt with the threshold issue of whether the fifth amendment privilege had been properly asserted so as to allow the district court to make a reasonable assessment of the risk of incrimination." App. 4a (footnote omitted). This as-

---

[11] Even if the Fifth Amendment does not require a judicial determination and an opportunity to respond under the circumstances of this case, petitioner urges the Court to impose such a requirement in the exercise of its supervisory power over the lower federal courts. Petitioner submits, as an alternative ground for granting the writ, that the court of appeals' decision so far sanctioned a departure by the district court from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision. Sup. Ct. R. 17.1(a).

[12] These decisions rest, in turn, upon this Court's holding in *Baxter* v. *Palmigiano*, 425 U.S. 308, 317-18 (1976), that a civil defendant's invocation of his Fifth Amendment privilege cannot, without more, suffice for judgment against him, although the invocation may give rise to an adverse inference. *See Pagel, Inc.* v. *SEC*, 803 F.2d 942, 946-47 (8th Cir. 1986).

serted distinction ignores the clear language of the two decisions.

In *Bathalter*, the defendant admitted the complaint's jurisdictional allegations, pleaded lack of knowledge to an additional allegation, and invoked the Fifth Amendment privilege in response to all remaining allegations. The Seventh Circuit "agree[d] with the implicit finding of the district court that Bathalter's assertion of the privilege in his answer, though not detailed, was sufficient and valid." *Id.* at 927 n.5.

The defendant in *Rogers* filed no answer at all; he merely notified the district court by letter that he would decline to respond to the civil contempt charges against him. 776 F.2d at 610. The Sixth Circuit declared:

> Instead of asserting [the privilege] in general fashion by letter *the better procedure would have been for Mr. Webster to have filed a formal answer or response in which he asserted the privilege as to each averment of Mr. Rogers which called for an admission or denial under Rule 8(b).* Nonetheless, it is clear that Mr. Webster was invoking the privilege, and the District Court did not rule that his method of doing so was improper.

Id. at 611 n.4 (emphasis added). Stefanou did precisely what *Rogers* counsels: he filed a formal answer in which he asserted his Fifth Amendment privilege in response to each allegation in North River's complaint.[13]

---

[13] *Rogers* and *Bathalter* implicitly recognize that a refusal to answer a series of specific allegations is not, as the court of appeals held, an improper "blanket" assertion of the privilege. In such a case, the court possesses all of the information it needs to determine whether an answer to a particular allegation could "furnish a link in the chain of evidence needed to prosecute." *Hoffman* v. *United States*, 341 U.S. at 486. An improper "blanket" assertion occurs only where a witness or party declares, before he is questioned, that he will not answer *any* questions. In that case, "a reviewing court cannot possibly 'anticipate every question that

The court of appeals' basis for distinguishing *Rogers* and *Bathalter* cannot withstand scrutiny. Despite its disclaimer, the Fourth Circuit's decision is squarely in conflict with the decisions of the Sixth and Seventh Circuits. The Court should grant the petition for writ of certiorari to resolve this conflict.

CONCLUSION

For the foregoing reasons, petitioner respectfully submits that the petition for writ of certiorari should be granted.

Respectfully submitted,

PETER J. KAHN
Counsel of Record
TERRENCE O'DONNELL
JOHN D. CLINE
WILLIAMS & CONNOLLY
Hill Building
839 17th Street, N.W.
Washington, D.C. 20006
(202) 331-5000
Attorneys for Petitioner
Peter Stefanou

March 18, 1988

---

might be asked and conclude that each would present a distinct possibility of self-incrimination if answered.'" *United States* v. *Moore*, 682 F.2d 853, 856 n.1 (9th Cir. 1982) (quoting *United States* v. *Malnik*, 489 F.2d 682, 686 (5th Cir.), *cert. denied*, 419 U.S. 826 (1974)). Here, the district court had before it North River's allegations and could easily have determined—as *Hoffman* requires it to do, *see* 341 U.S. at 486—whether answers to those allegations would pose a threat of self-incrimination to Stefanou.

APPENDICES

APPENDIX A

UNITED STATES COURT OF APPEALS
FOURTH CIRCUIT

No. 87-2548

NORTH RIVER INSURANCE COMPANY, INC.,
Plaintiff-Appellee,

v.

PETER STEFANOU,
Defendant-Appellant,

and

FRANK & COMPANY, PC; ROBERT H. FRANK; HAL L. YOUNG; ARTHUR J. EARLY; MARY BOYLE ARMSTRONG; TERRY A. ANDOLSHEK; PATRICIA A. COYLE; LAWRENCE GOLDMAN; J. MILLER,
Defendants.

Argued July 9, 1987

Decided Oct. 16, 1987

John DeWitt Cline (Terrence O'Donnell, Williams & Connolly, Washington, D.C., on brief), for defendant-appellant.

Charles Irwin Hadden (Wallace A. Christensen, Ellen M. Vollinger, Ross, Dixon & Masback, Washington, D.C., on brief), for plaintiff-appellee.

Before HALL and WILKINS, Circuit Judges, and G. ROSS ANDERSON, Jr., United States District Judge for the District of South Carolina, sitting by designation.

WILKINS, Circuit Judge:

Peter Stefanou appeals from the district court's entry of judgment on the pleadings for North River Insurance Company, Inc. (North River) after Stefanou refused to respond to the allegations of the complaint, and instead attempted to assert a fifth amendment claim against self-incrimination. We affirm.

I.

North River filed an action for a declaratory judgment seeking rescission of three professional liability insurance policies. Named as defendants were the accounting firm of Frank & Company, P.C. (previously known as Frank, Stefanou & Company); and Stefanou and eight other individuals, all of whom were partners or employees of the firm.[1] North River sought rescission of the policies issued to Frank & Company on grounds of misrepresentations in the policy applications. It alleged that Stefanou and a client, Edward Markowitz, had conspired to create more than $500,000,000.00 in fradulent tax deductions for tax investors and thus had misrepresented that they did not know of existing circumstances that might give rise to claims.

In April, 1985 Markowitz pled guilty to federal charges arising from his involvement in the fraudulent tax scheme. In June, 1986 Stefanou pled guilty to charges of income tax evasion, preparing a false tax return in relation to the Markowitz scheme, and preparing a false tax return in another related tax fraud scheme.

---

[1] Pursuant to a settlement, North River dismissed its complaint against all parties other than Stefanou on March 18, 1987.

In exchange for his plea, Stefanou and Frank & Company received immunity from further prosecution by the United States Attorney's Office for the Southern District of New York for federal criminal violations arising from involvement with certain named companies. They also received immunity from the Department of Justice from any further federal criminal tax prosecutions based on involvement with those companies. The immunity granted did not extend to prosecution in state court nor to prosecution by the Department of Justice for non-tax-related offenses.

All defendants except Stefanou timely filed a joint answer to North River's complaint. Stefanou responded only by reference in a footnote at the end of the opening sentence of the answer, stating that "[d]efendant Peter Stefanou, upon the advice of counsel, respectfully declines to answer the allegations set forth in plaintiff's complaint on the basis of his constitutional rights." Stefanou's fifth amendment claim was addressed to the entire complaint, including allegations of jurisdiction, venue, the existence of Stefanou's firm and his position with it. Stefanou gave similar responses in the discovery process when requests for admissions were served on him.

North River moved for judgment on the pleadings as to Stefanou. During the hearing on the motion, Stefanou did not seek to amend or otherwise alter his position. Instead, the record reflects that Stefanou continued his refusal to respond to the complaint, even to allegations reciting his guilty plea which was a matter of public record. The district court concluded that the fifth amendment privilege was not properly invoked and granted judgment on the pleadings against Stefanou.

II.

The failure to deny an allegation in a pleading to which a responsive pleading is required constitutes an admission of that allegation. Fed.R.Civ.P. 8(d). However, when

Stefanou's motion for reconsideration, App. 25a, ignoring his offer to replead if the court would rule as to which of the allegations it considered to be potentially incriminating and which it did not, C.A. 146. The district court made no finding that Stefanou had asserted his privilege in bad faith. No evidence was introduced against Stefanou, and he never admitted any of the allegations in North River's complaint.[5]

The court of appeals affirmed the district court's ruling in a split decision. Citing Fed. R. Civ. P. 8(d), the majority noted that "[t]he failure to deny an allegation in a pleading to which a responsive pleading is required constitutes an admission of that allegation." App. 3a. Although the majority conceded that "when properly invoked, the fifth amendment privilege against self-incrimination . . . can avoid the operation of Rule 8(d)," App. 3a-4a, it asserted that Stefanou's "blanket refusal to respond was not sufficient" to invoke the privilege, App. 5a. Thus, the court of appeals affirmed the district court's conclusion that *all* allegations in the complaint were properly deemed admitted, even those allegations, essential to North River's claim, with obvious potential to incriminate if answered.

In dissent, Judge K.K. Hall found Stefanou's invocation of the privilege sufficient and declared that "both the district court and the majority have ignored settled law in this Circuit." App. 6a.

---

for rescission of the insurance policies, since it was Stefanou's alleged relations with Markowitz that, according to North River, had not been disclosed in the applications for insurance. App. 40a-41a.

[5] North River dismissed the action pursuant to settlement as to all defendants other than Stefanou. App. 2a; C.A. 198. None of these defendants was a party to the appeal, and none is a party in this Court.

REASONS FOR GRANTING THE WRIT

The Court should grant the writ because (1) the court of appeals has wrongly decided an important question of federal law that has not been, but should be, settled by this Court, and (2) the decision of the court of appeals conflicts with decisions by the United States Courts of Appeals for the Sixth and Seventh Circuits on the same matter.

I. THE COURT OF APPEALS DECIDED AN IMPORTANT QUESTION OF FEDERAL LAW THAT HAS NOT BEEN, BUT SHOULD BE, SETTLED BY THIS COURT.

The Fourth Circuit wrongly decided an important question of federal law that has not been, but should be, settled by this Court: Whether judgment may be rendered against a civil defendant on the ground that he invoked his Fifth Amendment privilege too broadly in response to the complaint, where (a) it is undisputed that answers to the complaint's key substantive allegations could tend to incriminate the defendant, (b) the court has not determined whether answers to other allegations in the complaint could tend to incriminate the defendant or constitute a waiver of the privilege, (c) the defendant has not acted in bad faith, and (d) the defendant is not permitted to replead.[6]

---

[6] The court of appeals decided this question in part on the ground that Stefanou had not timely asserted his right to replead before the district court. App. 6a. In fact, as Stefanou pointed out to the court of appeals, he *did* raise the point before the district court; in his motion for reconsideration, Stefanou declared that he "stands ready to amend his Answer, invoking the privilege where the Court deems appropriate and responding where the Court finds (1) that the response could not possibly tend to incriminate him, and (2) that the response would not waive Mr. Stefanou's privilege." C.A. 146. The district court never determined which allegations in North River's complaint could tend to incriminate Stefanou and which could not, and Stefanou was therefore unable to amend his answer

The decision of the court of appeals places civil defendants with potential criminal liability in extraordinary peril. Either they can invoke the Fifth Amendment privilege and risk immediate loss of the case if the privilege is later overruled as having been too broadly asserted (as happened to Stefanou), or they can respond to the complaint's allegations and risk incriminating themselves and waiving the privilege.[7] An incorrect judgment can be costly; Stefanou, for example, has lost millions of dollars in insurance coverage. This choice, with little or no margin for error, imposes an impermissible burden on civil defendants' Fifth Amendment rights. Moreover, the issue is likely to recur often in light of the frequency of related civil and criminal proceedings.[8]

---

without risking incrimination and waiver of the privilege. In light of this clear statement by Stefanou that he would replead if the district court would rule on his invocation of the privilege, the court of appeals' assertion that he did not raise the point in the trial court is inexplicable.

[7] In *Rogers* v. *United States*, 340 U.S. 367, 373 (1951), this Court held that one who testifies as to some incriminating aspects of a matter may not invoke the Fifth Amendment privilege as to other aspects. Thus, if Stefanou had responded to some allegations of the complaint, mistakenly thinking them non-incriminating, he could well have discovered later that he had waived his privilege as to all related allegations. "[G]iven the somewhat indistinct boundaries of the 'waiver' doctrine," Stefanou's broad invocation of the privilege "would seem to have been no more than a prudent assertion of [his] rights." *United States* v. *Yurasovich*, 580 F.2d 1212, 1221 (3d Cir. 1978).

[8] The prevalence of such cases is reflected by the large number of recent appellate decisions addressing issues that arise when the Fifth Amendment privilege is asserted in civil litigation. *See, e.g.*, *Pillsbury Co.* v. *Conboy*, 459 U.S. 248 (1983); *United States* v. *Kordel*, 397 U.S. 1 (1970); *Pagel, Inc.* v. *SEC*, 803 F.2d 942 (8th Cir. 1986); *Rogers* v. *Webster*, 776 F.2d 607 (6th Cir. 1985); *Rosebud Sioux Tribe* v. *A & P Steel, Inc.*, 733 F.2d 509 (8th Cir.), *cert. denied*, 469 U.S. 1072 (1984); *Brinks, Inc.* v. *City of New York*, 717 F.2d 700 (2d Cir. 1983); *National Acceptance Co.* v. *Bathalter*, 705 F.2d 924 (7th Cir. 1983); *In re Folding Carton*

This Court has never addressed the precise question presented here. In other contexts, however, the Court has intimated that a person asserting the Fifth Amendment privilege should receive a preliminary determination as to the propriety of the invocation and an opportunity to respond before being penalized for asserting the privilege. In *Quinn* v. *United States*, 349 U.S. 155 (1955), for example, the Court reversed a conviction for contempt of Congress on the ground that the alleged contemnor, who had asserted the Fifth Amendment, "was never confronted with a clear-cut choice between compliance and non-compliance, between answering the question and risking prosecution for contempt." *Id.* at 166; *cf. Maness* v. *Meyers*, 419 U.S. 449, 461 (1975) (noting that "pre-compliance review [for a witness through contempt and appeal] is particularly appropriate where the Fifth Amendment privilege against self-incrimination is involved") (footnote omitted). And in *Hoffman* v. *United States*, the Court concluded that a grand jury witness

> is not exonerated from answering merely because he declares that in doing so he would incriminate himself—his say-so does not of itself establish the hazard of incrimination. *It is for the court to say whether his silence is justified . . . and to require him to answer if it clearly appears to the court that he is mistaken.*

341 U.S. at 486 (emphasis added) (citations and quotation omitted).[9]

Antitrust Litigation, 609 F.2d 867 (7th Cir. 1979); *In re Master Key Litigation*, 507 F.2d 292 (9th Cir. 1974); Heidt, *The Conjurer's Circle—The Fifth Amendment Privilege in Civil Cases*, 91 Yale L.J. 1062 (1982); Wolfson, *Civil Discovery and the Privilege Against Self-Incrimination*, 15 Pac. L.J. 785 (1984).

[9] In *Rogers* v. *Webster*, 776 F.2d 607 (6th Cir. 1985), where a civil defendant invoked his Fifth Amendment privilege in response to the complaint, the Sixth Circuit declared that "if [the defendant's] assertion of privilege had been overruled, we believe he would have been entitled then to an opportunity to respond to the con-

The Court's decision in *Garner* v. *United States*, 424 U.S. 648 (1976), is also instructive. In *Garner*, the Court concluded that a taxpayer who improperly asserted the Fifth Amendment on his tax return could be prosecuted for willful failure to file a return under 26 U.S.C. § 7203, without a preliminary ruling on the privilege and an opportunity to reconsider. *See id.* at 663-65. But because § 7203 requires proof of willfulness, the Court found that a good-faith but erroneous assertion of the privilege would preclude conviction. *See id.* at 663 n.18; *United States* v. *Murdock*, 290 U.S. 389, 397 (1933).[10]

The requirement that willfulness be proven under § 7203 was the key to the Court's holding in *Garner*. *See* 424 U.S. at 666 (Marshall, J., concurring); *United States* v. *Grabinski*, 558 F. Supp. 1324, 1333 (D. Minn. 1983), *modified on other grounds*, 727 F.2d 681 (8th Cir. 1984). Under the ruling of the Fourth Circuit in this case, by contrast, a civil defendant can have judgment rendered against him without any finding of bad faith or willfulness, without the court determining whether answers to specific allegations could tend to incriminate him or constitute a waiver of the privilege, and without an opportunity to reconsider his assertion of the privilege and respond on the merits.

---

tempt charges of his adversary." *Id.* at 611-12. The court correctly noted that a person asserting the Fifth Amendment privilege in a judicial proceeding "ordinarily 'receives a judicial ruling at that time on the validity of his claim, and he has an opportunity to reconsider it before being [penalized] for refusal to answer.'" *Id.* at 612 (brackets in original) (quoting *Garner* v. *United States*, 424 U.S. 648, 663 (1976)). *Rogers* concluded that "[n]ot affording one who asserts the privilege an opportunity to answer, once his claim of privilege has been rejected, is to penalize him merely for asserting the privilege." 776 F.2d at 612.

[10] Moreover, the Court noted in *Garner* that the taxpayer would usually receive a preliminary ruling on his privilege from the IRS. *See* 424 U.S. at 664 n.19. Thus, the taxpayer ordinarily would have an opportunity to reconsider the privilege before prosecution.

This Court has never decided whether a civil defendant can be penalized in this manner for invoking the Fifth Amendment too broadly. The writ of certiorari should issue so that the Court can resolve this important question.[11]

II. THE COURT OF APPEALS' DECISION CONFLICTS WITH DECISIONS BY THE SIXTH AND SEVENTH CIRCUITS.

The Fourth Circuit's decision conflicts with decisions of the Sixth and Seventh Circuits holding that judgment on the pleadings may not be rendered against a civil defendant solely because he invokes his Fifth Amendment privilege against self-incrimination in response to the complaint. *See Rogers* v. *Webster*, 776 F.2d 607, 611 (6th Cir. 1985); *National Acceptance Co.* v. *Bathalter*, 705 F.2d 924, 932 (7th Cir. 1983).[12]

The court of appeals purported to distinguish *Rogers* and *Bathalter* on the ground that "[n]either case dealt with the threshold issue of whether the fifth amendment privilege had been properly asserted so as to allow the district court to make a reasonable assessment of the risk of incrimination." App. 4a (footnote omitted). This as-

---

[11] Even if the Fifth Amendment does not require a judicial determination and an opportunity to respond under the circumstances of this case, petitioner urges the Court to impose such a requirement in the exercise of its supervisory power over the lower federal courts. Petitioner submits, as an alternative ground for granting the writ, that the court of appeals' decision so far sanctioned a departure by the district court from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision. Sup. Ct. R. 17.1(a).

[12] These decisions rest, in turn, upon this Court's holding in *Baxter* v. *Palmigiano*, 425 U.S. 308, 317-18 (1976), that a civil defendant's invocation of his Fifth Amendment privilege cannot, without more, suffice for judgment against him, although the invocation may give rise to an adverse inference. *See Pagel, Inc.* v. *SEC*, 803 F.2d 942, 946-47 (8th Cir. 1986).

serted distinction ignores the clear language of the two decisions.

In *Bathalter*, the defendant admitted the complaint's jurisdictional allegations, pleaded lack of knowledge to an additional allegation, and invoked the Fifth Amendment privilege in response to all remaining allegations. The Seventh Circuit "agree[d] with the implicit finding of the district court that Bathalter's assertion of the privilege in his answer, though not detailed, was sufficient and valid." *Id.* at 927 n.5.

The defendant in *Rogers* filed no answer at all; he merely notified the district court by letter that he would decline to respond to the civil contempt charges against him. 776 F.2d at 610. The Sixth Circuit declared:

> Instead of asserting [the privilege] in general fashion by letter *the better procedure would have been for Mr. Webster to have filed a formal answer or response in which he asserted the privilege as to each averment of Mr. Rogers which called for an admission or denial under Rule 8(b).* Nonetheless, it is clear that Mr. Webster was invoking the privilege, and the District Court did not rule that his method of doing so was improper.

Id. at 611 n.4 (emphasis added). Stefanou did precisely what *Rogers* counsels: he filed a formal answer in which he asserted his Fifth Amendment privilege in response to each allegation in North River's complaint.[13]

---

[13] *Rogers* and *Bathalter* implicitly recognize that a refusal to answer a series of specific allegations is not, as the court of appeals held, an improper "blanket" assertion of the privilege. In such a case, the court possesses all of the information it needs to determine whether an answer to a particular allegation could "furnish a link in the chain of evidence needed to prosecute." *Hoffman* v. *United States*, 341 U.S. at 486. An improper "blanket" assertion occurs only where a witness or party declares, before he is questioned, that he will not answer *any* questions. In that case, "a reviewing court cannot possibly 'anticipate every question that

The court of appeals' basis for distinguishing *Rogers* and *Bathalter* cannot withstand scrutiny. Despite its disclaimer, the Fourth Circuit's decision is squarely in conflict with the decisions of the Sixth and Seventh Circuits. The Court should grant the petition for writ of certiorari to resolve this conflict.

CONCLUSION

For the foregoing reasons, petitioner respectfully submits that the petition for writ of certiorari should be granted.

Respectfully submitted,

PETER J. KAHN
Counsel of Record
TERRENCE O'DONNELL
JOHN D. CLINE
WILLIAMS & CONNOLLY
Hill Building
839 17th Street, N.W.
Washington, D.C. 20006
(202) 331-5000
Attorneys for Petitioner
Peter Stefanou

March 18, 1988

---

might be asked and conclude that each would present a distinct possibility of self-incrimination if answered.'" *United States* v. *Moore*, 682 F.2d 853, 856 n.1 (9th Cir. 1982) (quoting *United States* v. *Malnik*, 489 F.2d 682, 686 (5th Cir.), *cert. denied*, 419 U.S. 826 (1974)). Here, the district court had before it North River's allegations and could easily have determined—as *Hoffman* requires it to do, *see* 341 U.S. at 486—whether answers to those allegations would pose a threat of self-incrimination to Stefanou.

APPENDICES

APPENDIX A

UNITED STATES COURT OF APPEALS
FOURTH CIRCUIT

No. 87-2548

NORTH RIVER INSURANCE COMPANY, INC.,
Plaintiff-Appellee,

v.

PETER STEFANOU,
Defendant-Appellant,

and

FRANK & COMPANY, PC; ROBERT H. FRANK; HAL L. YOUNG; ARTHUR J. EARLY; MARY BOYLE ARMSTRONG; TERRY A. ANDOLSHEK; PATRICIA A. COYLE; LAWRENCE GOLDMAN; J. MILLER,
Defendants.

Argued July 9, 1987

Decided Oct. 16, 1987

John DeWitt Cline (Terrence O'Donnell, Williams & Connolly, Washington, D.C., on brief), for defendant-appellant.

Charles Irwin Hadden (Wallace A. Christensen, Ellen M. Vollinger, Ross, Dixon & Masback, Washington, D.C., on brief), for plaintiff-appellee.

Before HALL and WILKINS, Circuit Judges, and G. ROSS ANDERSON, Jr., United States District Judge for the District of South Carolina, sitting by designation.

WILKINS, Circuit Judge:

Peter Stefanou appeals from the district court's entry of judgment on the pleadings for North River Insurance Company, Inc. (North River) after Stefanou refused to respond to the allegations of the complaint, and instead attempted to assert a fifth amendment claim against self-incrimination. We affirm.

I.

North River filed an action for a declaratory judgment seeking rescission of three professional liability insurance policies. Named as defendants were the accounting firm of Frank & Company, P.C. (previously known as Frank, Stefanou & Company); and Stefanou and eight other individuals, all of whom were partners or employees of the firm.[1] North River sought rescission of the policies issued to Frank & Company on grounds of misrepresentations in the policy applications. It alleged that Stefanou and a client, Edward Markowitz, had conspired to create more than $500,000,000.00 in fradulent tax deductions for tax investors and thus had misrepresented that they did not know of existing circumstances that might give rise to claims.

In April, 1985 Markowitz pled guilty to federal charges arising from his involvement in the fraudulent tax scheme. In June, 1986 Stefanou pled guilty to charges of income tax evasion, preparing a false tax return in relation to the Markowitz scheme, and preparing a false tax return in another related tax fraud scheme.

---

[1] Pursuant to a settlement, North River dismissed its complaint against all parties other than Stefanou on March 18, 1987.

In exchange for his plea, Stefanou and Frank & Company received immunity from further prosecution by the United States Attorney's Office for the Southern District of New York for federal criminal violations arising from involvement with certain named companies. They also received immunity from the Department of Justice from any further federal criminal tax prosecutions based on involvement with those companies. The immunity granted did not extend to prosecution in state court nor to prosecution by the Department of Justice for non-tax-related offenses.

All defendants except Stefanou timely filed a joint answer to North River's complaint. Stefanou responded only by reference in a footnote at the end of the opening sentence of the answer, stating that "[d]efendant Peter Stefanou, upon the advice of counsel, respectfully declines to answer the allegations set forth in plaintiff's complaint on the basis of his constitutional rights." Stefanou's fifth amendment claim was addressed to the entire complaint, including allegations of jurisdiction, venue, the existence of Stefanou's firm and his position with it. Stefanou gave similar responses in the discovery process when requests for admissions were served on him.

North River moved for judgment on the pleadings as to Stefanou. During the hearing on the motion, Stefanou did not seek to amend or otherwise alter his position. Instead, the record reflects that Stefanou continued his refusal to respond to the complaint, even to allegations reciting his guilty plea which was a matter of public record. The district court concluded that the fifth amendment privilege was not properly invoked and granted judgment on the pleadings against Stefanou.

II.

The failure to deny an allegation in a pleading to which a responsive pleading is required constitutes an admission of that allegation. Fed.R.Civ.P. 8(d). However, when

properly invoked, the fifth amendment privilege against self-incrimination, which applies to civil proceedings as well as criminal, can avoid the operation of Rule 8(d). The privilege applies not only at trial but also at the pleading stage. *In re Sterling-Harris Ford, Inc.*, 315 F.2d 277 (7th Cir.), *cert. denied*, 375 U.S. 814, 84 S.Ct. 46, 11 L.Ed.2d 50 (1963). However, the mere "blanket refusal to answer questions does not suffice to raise constitutional questions." *United States v. Carroll*, 567 F.2d 955, 957 (10th Cir.1977) (citing *United States v. Malnik*, 489 F.2d 682, 685 (5th Cir.), *cert. denied*, 419 U.S. 826, 95 S.Ct. 44, 42 L.Ed.2d 50 (1974)). Nor does a proper invocation of the privilege mean that a defendant is excused from the requirement to file a responsive pleading; he is obliged to answer those allegations that he can and to make a specific claim of the privilege as to the rest. 5 C. Wright & A. Miller, Federal Practice and Procedure § 1280, at 360 (1969).

Stefanou argues that his invocation of the privilege was proper under *Rogers v. Webster*, 776 F.2d 607 (6th Cir.1985), and *National Acceptance Co. of America v. Bathalter*, 705 F.2d 924 (7th Cir.1983). We disagree. Neither *Rogers* nor *National Acceptance* is dispositive of the issue presented here. Neither case dealt with the threshold issue of whether the fifth amendment privilege had been properly asserted so as to allow the district court to make a reasonable assessment of the risk of incrimination.[2] The issue here is whether Stefanou properly asserted his privilege, so that the rules of civil procedure "give way in order to protect the defendant's constitutional right to avoid self-incrimination," *Rogers*, 776 F.2d at 611 (quoting *National Acceptance*, 705 F.2d

---

[2] By dictum the court in *Rogers* expressed doubt that the contemner, Webster, had properly asserted the privilege but for purposes of its decision assumed that he had since "the District Court did not rule that his method of doing so was improper." *Rogers*, 776 F.2d at 611 n. 4.

at 926), or whether Stefanou chose a strategy that effectively negated a fair balancing of his interests against the interests of those pursuing a claim against him, and the interests of society in the expeditious resolution of litigation.

The privilege against self-incrimination, one of our most cherished fundamental rights, is jealously guarded by the courts. It protects an individual not only from involuntarily becoming a witness against himself in a criminal proceeding but also from answering specific allegations in a complaint or filing responses to interrogatories in a civil action where the answers might incriminate him in future criminal actions. But for one to invoke this privilege the party claiming it must not only affirmatively assert it, he must do so with sufficient particularity to allow an informed ruling on the claim. Under the circumstances of this case, a blanket refusal to respond was not sufficient. *United States v. Pierce*, 561 F.2d 735, 741 (9th Cir.1977), *cert. denied*, 435 U.S. 923, 98 S.Ct. 1486, 55 L.Ed.2d 516 (1978); *accord United States v. Zappola*, 646 F.2d 48, 53 (2d Cir.1981), *conviction aff'd on remand*, 677 F.2d 264 (2d Cir.), *cert. denied*, 459 U.S. 866, 103 S.Ct. 145, 74 L.Ed.2d 122 (1982); *United States v. Goodwin*, 625 F.2d 693, 701 (5th Cir.1980).

Stefanou incorrectly argues that the district court erred in failing to pierce his blanket assertion of privilege to determine its relative merits. A party wishing in good faith to assert the privilege must do so "with respect to particular [allegations]," thereby allowing the trial judge to determine the propriety of each refusal. *General Dynamics Corp. v. Selb Manufacturing Co.*, 481 F.2d 1204, 1212 (8th Cir.1973), *cert. denied*, 414 U.S. 1162, 94 S.Ct. 926, 39 L.Ed.2d 116 (1974) (citing *Hoffman v. United States*, 341 U.S. 479, 486, 71 S.Ct. 814, 818, 95 L.Ed. 1118 (1951)). The privilege also may be asserted and preserved in the course of discovery proceed-

ings, Fed.R.Civ.P. 26(c), but in specifics sufficient to provide the court with a record upon which to decide whether the privilege has been properly asserted as to each question. *United States v. Gordon*, 634 F.Supp. 409, 418 (Ct.Int'l Trade 1986).

The district court correctly ruled that the privilege was not properly invoked. Stefanou's potential for criminal liability had been narrowed significantly by the guilty plea already entered. Further concerns could have been met by good-faith responses tailored to address specific allegations in the complaint. Instead, he chose a course of action which left the district court with no reasonable alternative other than to enter judgment against him. Fed.R.Civ.P. 8(d).

III.

Stefanou argues in the alternative that the case should be remanded to the district court with instructions to allow him to amend. The argument might be more persuasive had he timely raised it before the district court. We accordingly decline to consider it for the first time on appeal. *United States v. One 1971 Mercedes Benz*, 542 F.2d 912, 915 (4th Cir.1976).

AFFIRMED.

R.K. HALL, Circuit Judge, dissenting:

I cannot agree with the majority's conclusion that Stefanou improperly invoked the privilege against self-incrimination in his responses to the pleadings in this action. For this reason, I respectfully dissent.

In my view, both the district court and the majority have ignored settled law in this Circuit. In *Mills v. United States*, 281 F.2d 736 (4th Cir.1960), we held that invocation of the privilege is sufficient if the objection is stated in a language that the court could reasonably be

expected to understand as an attempt to invoke the privilege. Clearly the district court was aware and acknowledged that Stefanou was attempting to invoke the privilege. Thus, the district court erred when it ruled that the privilege was not properly invoked and should not have entered judgment on the pleadings.

The government contends that there is another basis on which to affirm the district court opinion. Stefanou declined to respond to the request for admissions on the basis of his constitutional rights. Local Rule 11.1(D) establishes a 15-day time limit in which to object to request for admissions or they are deemed to be admitted. Stefanou responded to the request for admissions within the 30-day time limit as required by Fed.R.Civ.P 36. North River filed a motion with the magistrate to have the request deemed admitted. Stefanou opposed this motion, however, the magistrate granted it. Stefanou then moved for reconsideration but the district court denied Stefanou's motion, concluding that the judgment on the pleadings against Stefanou rendered reconsideration moot. If we find that Stefanou properly invoked the privilege against self-incrimination, then the issue is no longer moot. However, we cannot affirm the district court opinion on this basis because the district court made no specific ruling on Stefanou's motion for reconsideration.

Having found that Stefanou's invocation of the fifth amendment privilege against self-incrimination was properly invoked in his answers to the pleadings and discovery, I would reverse and remand this case to the district court for further proceedings. On remand, I would instruct the district court to decide if Stefanou's response to the request for admissions was timely filed.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF VIRGINIA
Alexandria Division

Civil Action No. 86-1173-A

NORTH RIVER INSURANCE CO., INC.,
Plaintiff,

-vs-

FRANK & COMPANY, P.C., *et al.*,
Defendants.

Friday, February 20, 1987

Alexandria, Virginia

Transcript of motion proceedings in the above-captioned matter.

BEFORE:

The Honorable ALBERT V. BRYAN, JR., Judge
United States District Court

APPEARANCES:

For the Plaintiff:

JAMES E. GROSSBERG, ESQUIRE
1050 Connecticut Avenue, N.W.
Washington, D. C. 20036

[2]

For the Defendants:

CRAIG C. REILLY, ESQUIRE
MURPHY, MCGETTIGAN & WEST, P.C.
921 King Street
Alexandria, Virginia 22314

JOHN D. CLINE, ESQUIRE
TERENCE O'DONNELL, ESQUIRE
WILLIAMS & CONNOLLY
839 17th Street, N.W.
Washington, D. C.

[3] PROCEEDINGS

THE CLERK: Civil Action No. 86-1173-A, North River Insurance Company, Incorporated versus Frank & Company, P.C., et al.

THE COURT: This comes on on motion for leave to file motion to stay.

MR. GROSSBERG: We have got several motions before you. I believe the one that was filed first was a motion for judgment on the pleadings. It was filed last week and continued to this week. I think logically it makes the most sense to address that first.

THE COURT: All right.

MR. GROSSBERG: Our argument with respect to that motion is quite straightforward. Under the Federal Rules of Civil—

THE COURT: (Interposing) Well, let me ask you something that is a little peripheral to that. If you get judgment on the pleadings, can you do it against more than the one defendant? That wouldn't bind the other defendants, would it?

MR. GROSSBERG: I think that the facts that would be established by the admission by Mr. Stefanow would be usable by us against the other defendants.

THE COURT: How could it be? If he chooses not to defend the case, for example—that isn't the basis of your

[4] motion—but suppose he just let it go by default, would the others be precluded from defending and saying that we are entitled to be heard on the question of whether he made a material misrepresentation on that since you are trying to hold us liable. The fact that he doesn't choose to defend it or for some reason is precluded from defending it, why should that bind the other defendants?

MR. GROSSBERG: Well, I think that it would be an admission on his part. The way Rule 8(d) reads is that the facts that are alleged in the complaint are deemed admitted.

THE COURT: It wouldn't be a conclusive admission as far as they are concerned, though, would it?

MR. GROSSBERG: It would at least be some evidence against them, and in that situation I believe what would probably be appropriate is to enter the judgment against Stefanow and stay it as to the rest of the parties so that we could until such time as he would be able to testify, not invoke his privilege and that we would be able to proceed with our case fairly to judgment as the 4th Circuit has said in the Shaffer (phonetic) case.

THE COURT: All right.

MR. GROSSBERG: Our argument is quite straightforward with respect to the motion. Under Rule 8(d), the failure to deny an allegation constitutes an admission of that allegation. Defendant Stefanow refused to deny any of the [5] allegations of the complaint on the basis of his constitutional rights—

THE COURT: (Interposing) Excuse me. Where is the file on this case? Thank you.

Go ahead, sir.

MR. GROSSBERG: We recognize that a proper, and I emphasize the word proper invocation of the 5th Amendment can avoid the operation of Rule 8(d), but Mr. Stefanow's blanket assertion is not a proper invocation of the privilege and it can't preclude Rule 8(d) from taking effect.

What he should have done, and this is what the commentator suggests and what makes sense so that the Court can judge his 5th Amendment privilege, is to answer those allegations that he could, without incriminating himself and plead the 5th Amendment as to the rest.

The defendants claim that most of the allegations are not incriminating or have already been—excuse me—they claim they are incriminating and they would not answer on those grounds. We submit that they are not incriminating or have already been waived.

For this reason, Mr. Stefanow's response is not only improper but we believe that it's somewhat disingenuous and I think the best example of this is paragraph 25 of our complaint, we allege that Defendant Stefanow pled guilty in the Southern District of New York to various counts of tax [6] fraud. At page 7 of his papers filed with you, the Defendant Stefanow says he couldn't answer this allegation because it might lead to some other evidence, a link in the chain, and that would incriminate him and it would waive his privilege with respect to the entire area.

One page earlier, two paragraphs before that, he makes the very admission that he says he couldn't admit to. He says he did plead guilty in New York to the various counts of tax fraud. So I think the whole question here we are faced with a situation where he has asserted the 5th Amendment just to avoid answering allegations that are properly answerable and he is attempting to hide behind the 5th Amendment here, and make the insurance company jump through various hoops that they shouldn't have to be jumping through.

THE COURT: I think the issue on your motion for judgment on the pleadings is clear.

Do you want to address your motion for stay?

MR. GROSSBERG: Sure, Your Honor.

The North River has moved for a stay until the conclusion of the criminal proceedings or until all the applicable statute of limitations—

THE COURT: (Interposing) When might that be?

MR. GROSSBERG: Mr. Cline's papers suggests that that might be two years from now when the applicable statute of limitations run. But we are faced with a situation where [7] Mr. Markowitz (phonetic) and Mr. Stefanow have blocked our attempt to learn the relevant facts of this case by virtue of their pleading the 5th Amendment. We are not saying that they don't have a right to plead the 5th Amendment. We are just saying that we have a right to try our case fairly. Markowitz has pled guilty—

THE COURT: (Interposing) You want it to sit here for two years while the—

MR. GROSSBERG: (Interposing) It will be on your docket but it won't cause any other inconvenience, Your Honor. There are cases where it has sat for longer than that.

THE COURT: Not here.

MR. GROSSBERG: Well, Mr. Markowitz has pled guilty to a tax fraud, the largest tax fraud ever prosecuted, $445 million in phony tax deductions, and he admitted that he conspired with brokers, lawyers and accountants. We know that the defendant and his firm provided tax services and accounting services to Mr. Markowitz. The defendant, Mr. Stefanow, has also pled guilty to filing false tax returns. It's obvious that Markowitz and Stefanow's testimony is crucial to North River's ability to prove that Stefanow or Frank & Company was aware that a claim might be made against them at the time they filled out the insurance applications.

We have to be able to get the direct testimony of [8] these witnesses, and we have been blocked by virtue of the 5th Amendment assertion on their part. That's perfectly proper for them to do that. We are not contending that it doesn't apply in civil proceedings, but we are entitled to have our case proceed fairly to judgment as well. They can't use the 5th Amendment as a shield and

then turn around—from criminal prosecution—and then turn around and use it as a sword in their litigation with us.

THE COURT: Well, they didn't bring the litigation. You brought the litigation.

MR. GROSSBERG: Well, they are still using it against us, Your Honor, and the plaintiff-defendant distinction is ordinarily not well taken, I think. The Whalen (phonetic) case points that out. It's at footnote 10 of that decision. And it's especially meaningless in this case because they could have brought the litigation. It just happened to arise that way. We are here on a declaratory judgment action. We could have just as easily unilaterally rescinded the policy and then they would have been the ones who brought it forward.

The point is they are seeking to preserve their rights under the policy or the right they assert they have under the policy and that is the effect at which they are using the sword. They are trying to establish rights under a policy. We are entitled to be in Court and have our [9] questions answered and allow us to learn the facts of the case.

The Shaffer case, the 4th Circuit case that we cited in our brief, there was a claim and a counterclaim. The District Court entered judgment for the Government on both the claim and the counterclaim, so in effect it was entering judgment against the defendant. The 4th Circuit overturned that and said, "Don't penalize this guy because he asserted his 5th Amendment rights, but look for some other procedure that strikes a fair balance, that accommodates the interests of the parties, that allows it to proceed fairly to judgment." That's what we are asking for here.

We have been denied an opportunity to learn what this person who has admittedly pled guilty, his paper said. We know that that would constitute a basis for rescinding some of the policies but we need an opportu-

nity to question him and question Mr. Markowitz about their activities.

These two gentlemen are involved in what is perhaps the largest tax fraud ever. And the insurance company has been put in ths position of trying to make its case with its eyes closed and its hands tied behind its back because we can't get the evidence from the two key players in the whole situation.

THE COURT: You want to address your motion for reconsideration?

[10] Mr. GROSSBERG: Your Honor, if I could add just briefly two quick points on the stay: our opponents properly focused on the fact that you should be looking at the harm to the parties in this case. The only harm they assert, we think is laughable. They said this case is a stigma against the defendants. I don't see how this could possibly be a stigma against the defendants any more so than one of their partners pleading guilty to tax fraud, having his license revoked, and the underlying civil suit which North River is paying the fees for, by the way and will continue to pay the fees for, they have been accused in that suit of conspiring with Markowitz of committing fraud, of breaching their fiduciary duties.

This is only the icing on the cake. The cake is everything else. Their harm is certainly not available as an excuse for not granting a stay here.

The last point in that if you will bear with me one more second, Your Honor, is that they are not going to be able to get new insurance. These folks are uninsurable. Whatever this rescission act, whatever the result of this insurance action, they are not going to get new insurance. They are going to be in a position of having to say on an application that they have these existing claims against them, that a partner of a previous incarnation of the entity had his license revoked, that they have had insurance nonrenewed. [11] This action makes no difference with respect to their insurance and it's not about their new insurance at all.

THE COURT: I am inclined—on the motion for reconsideration of my order overruling the magistrate's order, let me hear from the defendants on that before I ask you to respond to it.

MR. REILLY: Good morning, Your Honor. Craig Reilly on behalf of the defendants.

I would like to introduce to the Court John Cline, who will be handling the matter on behalf of the defendants this morning.

THE COURT: Yes, sir.

MR. CLINE: Your Honor, our position on the motion for reconsideration is that there is simply no basis at this point to reconsider the Court's order entered Februray 13th.

THE COURT: Well, the plaintiffs may have gotten caught on that, even though you did tell them you were going to appeal the magistrate's order into calling off those depositions after the magistrate extended discovery; and then when I reversed that, they were in sort of a—it seems to me they were unfairly caught and had to cancel those depositions.

MR. CLINE: I understand their predicament. I would say this: It was brought on first by their belated initiation of discovery. Second, we did inform them that we [12] planned to appeal the magistrate's order. And third, and this point, even if it would have been appropriate perhaps to allow them a week beginning February 13th, at this point we have had the pretrial. We have submitted witness lists and exhibits. The trial date is less than a month from now. And to recommence discovery at this point it seems to me would throw things completely off track.

THE COURT: Do you want to address the motion for judgment on the pleadings? How can you deny or say it would incriminate you to admit that this Defendant Stefanow has pled guilty in the—I mean, that's a matter of public record. How is that going to incrimi-

nate him any more than the plea would incriminate him anyway?

MR. CLINE: The problem, Your Honor, is that the plea agreement doesn't protect him in all places for all potential offenses.

THE COURT: But the fact of the plea agreement, how can he say that that is going to incriminate him?

MR. CLINE: The problem is that the fact, admitting to the fact of the plea agreement may constitute, may be construed as an admission to the facts underlying the plea agreement or to certain peripheral—

THE COURT: (Interposing)—Of course it will, but how is he in a position to deny that? How can he say after he has pled guilty to the offense, even if it's overtime [13] parking, well, if you asked me did I plead guilty to overtime parking, that incriminates me? Criminally?

MR. CLINE: He's not denying it, Your Honor.

THE COURT: He has said he can't answer it because it would incriminate him.

MR. CLINE: That's correct, and I adhere to that—

THE COURT: (Interposing) That's facetious.

MR. CLINE: In any case, Your Honor, even if as to that averment or some other averment, for example, concerning the parties in this case, he did not properly invoke the privilege. And even if we were prepared to say that by admitting those things he would not waive any privilege, that doesn't begin to prove North River's case, and that's the underlying problem.

THE COURT: It does as to him, doesn't it?

MR. CLINE: No, it doesn't, I don't believe so. They have to prove that the defendants were at the time they filled out their application, aware of circumstances that could give rise to the claim. They haven't—admitting, for example, that Mr. Stefanow pled guilty to certain matters which incidentally were not related to Mr. Markowitz, admitting that he is familiar with the parties in this case, that doesn't even begin to make that claim

and the crucial allegations in their complaint which do pertain to Markowitz and to all kinds of alleged wrongdoing, as to those things, [14] there is absolutely no question that his invocation of the privilege is proper.

THE COURT: I'm not sure that it is at all. This footnote that he can't answer anything because it might tend to incriminate him in an answer, I don't think is a proper invocation of a 5th Amendment privilege, is it? It certainly isn't in any other circumstances.

MR. CLINE: Your Honor, he could have repeated that statement following each averment in the complaint. In that case it would be incumbent upon this Court to examine each assertion of the privilege and say as to some, that's correct; as to some, it isn't. The fact that he asserted it as to each allegation in the complaint through a single statement rather than through 76 repetitions of that statement or however many paragraphs there are, I don't think makes any difference.

THE COURT: Well, at least we would know there had been some consideration of each allegation as to whether it would or not. This way, you certainly couldn't refuse to go to a grand jury and say, "I'm not going to answer anything."

MR. CLINE: But I want to make it clear that he didn't do that. There is a distinction between refusing to respond and claim the privilege at all and claiming the privilege as Mr. Stefanow did as to a series of specific averments. He did not take a blanket 5th. He didn't refuse [15] to appear or refuse to answer. He answered. His answer consisted of a series of specific invocations of the 5th Amendment. This Court may find some of those invocations were improper. That certainly doesn't mean that the others were improper.

THE COURT: All right. Do you want to address the motion for stay?

MR. CLINE: The guiding principle on a motion for stay is simply that the party seeking the stay must prove by clear and convincing circumstances that the

burden that the State would impose on the other party is outweighed by the benefits to the party seeking the stay.

In this case the plaintiff is seeking a two-year, at least a two-year stay of its action. To say that that wouldn't impose a burden on the defendants I think is silly. It would impose a burden. This case is pending. They have to deal with it. They will have extreme difficulties finding insurance. And it is particularly unfair to saddle them with this lawsuit for two years when all North River has to do is nonsuit this case and refile it when it feels like it can make its case.

The effect on North River would be exactly the same. They plan to continue paying they say the defense costs in any case. They can refile it next year if they think they have a case or they can refile it the year after [16] that but to have this case hanging around for two years burdening the defendants, requiring them to report on their applications for additional insurance that there is litigation pending against them and other insurers seeking rescission, that is just not fair.

What they want to do, what our clients want to do is pursue this case to final judgment, to win it as they believe they can and to be done with it.

THE COURT: All right. Any response?

MR. GROSSBERG: Your Honor, I would just like to make a couple quick points: It's not necessarily two years that would be required for this stay. If Mr. Stefanow—

THE COURT: (Interposing) You say one of the things you want to get from the—is a grand jury transcript. What assurances do you have that you are going to get any grand jury transcripts just because the—you don't normally get grand jury transcripts even though the grand jury has rendered its indictment or the case has been tried.

MR. GROSSBERG: It's possible we won't get that but we understand there are going to be indictments

within the next three to six months. We have been advised of that.

Mr. Stefanow and Mr. Markowitz may testify. We could use the transcript of their trial testimony and this Court could use—

THE COURT: (Interposing) All of that is really [17] problematical, isn't it? I don't have any assurance of when this case will be tried.

MR. GROSSBERG: About the only assurance anyone has in this case is we are not able to get our information because of the Fifth Amendment. It's certainly a privilege that we respect and are willing to allow the defendants to assert but we shouldn't be penalized in our ability to prove our case because they are asserting it.

My point is that perhaps it won't be as long as Mr. Cline has just suggested, that it's two years, because they may testify before that date. We may be able to come back to the Court and say that we now have a waive of the privilege. We are ready to go ahead with this.

The second thing is, last Sunday we finally received some of the documents that we had been requesting. One of the documents as an affidavit of Peter Stefanow in which he further waives the privilege. It's an affidavit on Williams & Connolly pleadings paper; it's dated December '83. He said in there, "I am a certified public accountant partner in the accounting firm of Frank Stefanow and Company. Since September 1980 my firm has rendered various auditing, accounting and tax services on behalf of the plaintiff, TMG II.

TMG II is one of the entities for which Mr. Markowitz had pled guilty to filing a false tax return for the year 1980.

[18] This is precisely at the crux of our case. That's an allegation we made in our complaint that he provided those services. This is one of those allegations he says he can't answer because of his constitutional rights. Those rights are waived. We are entitled to ask him the ques-

tions about that. We are entitled to ask him the questions about the guilty plea.

Mr. Stefanow's papers themselves say that he can't answer those questions because he would waive those rights. I think he is playing fast and loose with the Court, Your Honor. That's why we haven't gotten an allegation-by-allegation denial because they couldn't do it. Virtually 50 of the 65 allegations or whatever there were in the complaint are ones that wouldn't have incriminated him, and this was an abuse of the invocation of the privilege to do it in the fashion that they did.

And the last point, Your Honor, is that there really is not much of a burden to the opposing side if there is a stay. Their insurability I have already addressed. There is not going to be ongoing litigation or ongoing expense. And we are going to be paying their defense costs in the underlying litigation.

THE COURT: I don't think that the 5th Amendment privilege was properly invoked by Stefanow. I don't think you can do it in this way with an asterisk to the answer to [19] the complaint, which says that—"declines to answer the allegations set forth in the complaint on the basis of his constitutional right." That's no invocation of the privilege. I think that the plaintiff is entitled to judgment on the pleadings as to Stefanow, but only as to Stefanow. I don't think the others can be bound by that. I will grant that motion.

The motion for stay will be denied. I am unwilling to leave this case on the docket on the problematical assurance that maybe in a year-and-a-half or two years the criminal action will be resolved to such an extent that the plaintiff can get the discovery it seeks. There is no requirement that they file suit, and there is no requirement that they file suit in this Court where we do not let matters stay very long on the docket and having filed suit, the case will proceed in accordance with the regular scheduling order.

If the plaintiff wants to dismiss his suit, that's its problem or its choice, but I don't have any basis upon which to stay this suit, and the motion for a stay will be denied.

I wil reconsider my order overruling the magistrate's order in that I will allow the taking, provided it's promptly done, of those depositions which have been noted for the time that intervened between the magistrate's order and my order which overruled the magistrate's order. [20] That's the only additional discovery I will allow. The motion for reconsideration will be granted to that extent.

MR. O'DONNELL: Your Honor, Terence O'Donnell for the defendants. May I bring to the Court's attention two points that I believe are very important with respect to the judgment on the pleadings?

THE COURT: I heard both sides on that now. I have really heard all I want to hear.

MR. O'DONNELL: Thank you, Your Honor.

(Whereupon, the proceedings in the above-captioned matter were concluded).

[21] CERTIFICATE OF OFFICIAL REPORTER

COMMONWEALTH OF VIRGINIA)
) ss.
CITY OF ALEXANDRIA)

I, EDWARD DONOVAN McCOY, Registered Professional Reporter and Official Court Reporter for the United States District Court for the Eastern District of Virginia, appointed pursuant to the provisions of Title 28, United States Code, Section 753, do hereby certify that I was authorized to report, and did so report in Stenotype, the foregoing proceedings;

THEREAFTER, my Stenotype notes were reduced to typewriting under my supervision; and I further certify that the pages herein numbered contain a true and correct transcription of my Stenotype notes taken herein.

DONE and signed, this —— day of ———, 19—, in the City of Alexandria, Commonwealth of Virginia.

EDWARD DONOVAN McCOY, RRP
Official Court Reporter

APPENDIX C

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
ALEXANDRIA DIVISION

Civil Action No. 96-1173-A

NORTH RIVER INSURANCE COMPANY, INC.,
Plaintiff,

v.

FRANK & COMPANY, P.C., *et al.*,
Defendants.

ORDER

For the reasons stated from the bench, the court concluding that the attempted invocation by the defendant Peter Stefanou of his Fifth Amendment right not to answer the allegation of the complaint was ineffective and improperly done, and being unwilling to stay the proceedings for an unascertainable time to allow the plaintiff to conduct its discovery, it is hereby ORDERED that:

1. The motion of the plaintiff for judgment on the pleadings is granted as to the defendant Peter Stefanou, but not as to the remaining defendants.

2. The motion of the plaintiff for a stay of these proceedings is denied.

3. The motion of the plaintiff for reconsideration of the court's order of February 13, 1987 is granted only to the extent that the court now allows the taking by

the plaintiff of the depositions which had been scheduled for the period between the magistrate's order of February 10, 1987 and the court's order of February 17, 1987.

/s/ Albert V. Bryan, Jr.
United States District Judge

Alexandria, Virginia
February 20th, 1987

APPENDIX D

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
ALEXANDRIA DIVISION

Civil Action No. 86-1173-A

NORTH RIVER INSURANCE COMPANY, INC.,
Plaintiff,

v.

FRANK & COMPANY, P.C., *et al.*,
Defendants.

ORDER

Upon consideration of the motion for reconsideration of the court's February 20, 1987 grant of judgment on the pleadings against the defendant Peter Stefanou, it is hereby

ORDERED that the motion for reconsideration is denied.

/s/ Albert V. Bryan, Jr.
United States District Judge

Alexandria, Virginia
March 6th, 1987

APPENDIX E

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 87-2548

NORTH RIVER INSURANCE COMPANY, INC.,
Plaintiff-Appellee

v.

PETER STEFANOU,
Defendant-Appellant

and

FRANK & COMPANY, PC; ROBERT H. FRANK; HAL L. YOUNG; ARTHUR J. EARLY; MARY BOYLE ARMSTRONG; TERRY A. ANDOLSHEK; PATRICIA A. COYLE; LAWRENCE GOLDMAN; J. MILLER,
Defendants

[Filed Oct. 16, 1987]

Appeal from the United States District Court
for the Eastern District of Virginia

JUDGMENT

THIS CAUSE came on to be heard on the record from the United States District Court for the Eastern District of Virginia, and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the said District Court appealed from, in this cause, be, and the same is hereby, affirmed.

/s/ John M. Greacen
Clerk

APPENDIX F

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 87-2548

NORTH RIVER INSURANCE CO., INC.,
Plaintiff-Appellee,

v.

PETER STEFANOU,
Defendant-Appellant,

and

FRANK & COMPANY, PC, *et al*,
Defendants.

On Petition for Rehearing with Suggestion for Rehearing In Banc

---

[Filed Dec. 21, 1987]

The appellant's petition for rehearing and suggestion for rehearing in banc were submitted to this Court. As no member of the Court requested a poll on the suggestion for rehearing in banc, and

As the panel considered the petition for rehearing and is of the opinion that it should be denied,

IT IS ORDERED that the petition for rehearing and suggestion for rehearing in banc are denied.

Entered at the direction of Judge Wilkins, with the concurrence of Judge Anderson. Judge Hall dissents.

For the Court:

/s/ John M. Greacen
Clerk

APPENDIX G

UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA

Civil Action No.

NORTH RIVER INSURANCE COMPANY, INC.
200 S. Wacker Drive
Chicago, Illinois 60606,
Plaintiff,

v.

FRANK & COMPANY, P.C., previously known as
FRANK, STEFANOU & CO.,
1360 Beverly Road
McLean, Virginia, 22101

Serve: Robert H. Frank
1360 Beverly Road
McLean, Virginia 22101,

PETER STEFANOU
1839 Baldwin Drive
McLean, Virginia 22101,

ROBERT H. FRANK, HAL L. YOUNG, ARTHUR J. EARLY,
MARY BOYLE ARMSTRONG, TERRY A. ANDOLSHEK,
PATRICIA A. COYLE, LAWRENCE GOLDMAN, and J. MILLER,
1360 Beverly Road
McLean, Virginia 22101,
Defendants.

COMPLAINT FOR DECLARATORY JUDGMENT

Plaintiff, North River Insurance Company, ("North River"), for its complaint against defendants named above, and each of them, alleges as follows:

JURISDICTION AND VENUE

1. Plaintiff brings this action, pursuant to 28 U.S.C. §§ 2201 and 2202, for a declaratory judgment that three accountants' professional liability insurance policies, each of which was issued to one or more of the defendants, be rescinded. In the alternative, plaintiff seeks a declaratory judgment rescinding two of the policies and the increases in the limits of liability under the third policy.

2. This Court's jurisdiction is invoked pursuant to 28 U.S.C. § 1332. There is complete diversity of citizenship between the parties, and the amount in controversy exceeds the sum of Ten Thousand Dollars ($10,000), exclusive of interest and costs.

3. Venue is proper in this Court, pursuant to 28 U.S.C. § 1391, in that the claims asserted arose in this district.

PARTIES

4. Plaintiff is a New Jersey corporation with its principal place of business in Chicago, Illinois. North River is engaged in the business of insurance and issues insurance policies, including accountants' professional liability insurance policies.

5. Defendant Frank & Company, P.C., ("Frank & Co."), is a certified public accounting firm located and doing business at 1360 Beverly Road, McLean, Virginia 22101. Until approximately June 1986, Frank & Co. did business as Frank, Stefanou & Co. Prior to January 1, 1985 Frank & Co. was a partnership organized under the laws of Virginia; after that date it was a professional corporation organized under the laws of Virginia. Frank & Co. purchased three successive accountant's professional liability insurance policies from North River. As used herein, "Frank & Co." refers to both that professional corporation, and its predecessors in business, Frank, Stefanou & Co. and Frank, Stefanou & Co., P.C.

6. Defendant Robert H. Frank has been either a partner or proprietor of Frank & Co. from at least as early as October 11, 1981 to the present (the "pertinent time period"). At all pertinent times, Frank was a named insured under the insurance policies issued to Frank & Co. by North River. Frank resides in and is a citizen of Virginia.

7. Defendant Peter Stefanou was, from at least as early as October 11, 1981 until approximately June 1986, a partner or proprietor of Frank & Co. Stefanou was a named insured under one or more of the insurance policies issued to Frank & Co. by North River. Stefanou resides in and is a citizen of Virginia.

8. Defendant Hal L. Young has been a partner or proprietor of Frank & Co. during at least some part of the pertinent time period. Young was a named insured under one or more of the insurance policies issued to Frank & Co. by North River. On information and belief, Young resides in and is a citizen of a state other than New Jersey or Illinois.

9. Arthur J. Early is a certified public accountant and has been an employee of Frank & Co. during at least some part of the pertinent time period. Early was a named insured under one or more of the insurance policies issued to Frank & Co. by North River. On information and belief, Early resides in and is a citizen of a state other than New Jersey or Illinois.

10. Mary Boyle Armstrong is a certified public accountant and has been an employee of Frank & Co. during at least some part of the pertinent time period. Armstrong was a named insured under one or more of the insurance policies issued to Frank & Co. by North River. On information and belief, Armstrong resides in and is a citizen of a state other than New Jersey or Illinois.

11. Terry A. Andolshek is a certified public accountant and has been an employee of Frank & Co. during at least some part of the pertinent time period. Andolshek was a named insured under one or more of the insurance policies issued to Frank & Co. by North River. On information and belief, Andolshek resides in and is a citizen of a state other than New Jersey or Illinois.

12. Patricia A. Coyle is a certified public accountant and has been an employee of Frank & Co. during at least some part of the pertinent time period. Coyle was a named insured under one or more of the insurance policies issued to Frank & Co. by North River. On information and belief, Coyle resides in and is a citizen of a state other than New Jersey or Illinois.

13. Lawrence Goldman is a certified public accountant and has been an employee of Frank & Co. during at least some of the pertinent time period. Goldman was a named insured under one or more of the insurance policies issued to Frank & Co. by North River. On information and belief, Goldman resides in and is a citizen of a state other than New Jersey or Illinois.

14. J. Miller is a certified public accountant and was an employee of Frank & Co. during part of the pertinent time period. Miller was a named insured under one or more of the insurance policies issued to Frank & Co. by North River. On information and belief, Miller resides in and is a citizen of a state other than New Jersey or Illinois.

BACKGROUND

15. Beginning in late 1980 or early 1981 and continuing through approximately 1984, Stefanou and Frank & Co. provided accounting services, including the preparation of tax returns, for one Edward Markowitz, and various limited partnerships formed and/or controlled by Markowitz. During this time, Markowitz generated more than $500,000,000 in false income tax deductions for in-

vestors in certain of his limited partnerships, and for customers of those limited partnerships. The fraudulent deductions were generated by sham transactions in government securities and in precious metal contracts. In some instances documents were prepared for transactions which in fact had never occurred; in other instances, documents were prepared to reflect transactions which had no economic substance and which had been entirely prearranged, were risk free and intended solely to generate paper documentation to support unfounded tax deductions.

16. One of the entities formed by Markowitz to provide these fictitious tax deductions was a limited partnership called TMG II. Frank & Co. provided accounting services to TMG II beginning in late 1980 or early 1981.

17. Prior to Frank & Co.'s engagement by Markowitz, Price-Waterhouse & Co. provided accounting services for Markowitz and for a number of Markowitz-controlled entities, including TMG II. In or about March 1981, Price-Waterhouse & Co. withdrew from the TMG II engagement and declined to sign the partnership's 1980 income tax return because, *inter alia*, it found no evidence that the transactions that generated the tax deductions listed on the return actually occurred and were not simply paper transactions. Defendants Frank & Co., Stefanou, and perhaps other defendants as well, knew the reason for Price-Waterhouse & Co.'s withdrawal at the time when Frank & Co. succeeded Price-Waterhouse & Co. as Markowitz's accountant. On information and belief, Frank & Co. and Stefanou nonetheless thereafter prepared the 1980 tax return for TMG II, which reflected a materially false and fraudulent loss of $8,509,101.

18. Another Markowitz-controlled entity for which Frank & Co. provided accounting services was a limited partnership called TMG Associates. Like TMG II, TMG Associates was a tax shelter that purported to generate

tax deductions through trading in United States government securities and precious metals futures contracts. The losses provided by TMG Associates were fictitious. In addition to providing fictitious tax losses to its limited partner investors, TMG Associates and related entities provided losses to customers, one of which was a limited partnership called Dominion Securities Group ("Dominion Securities").

19. In 1980 Dominion Securities obtained tax losses as a customer of a Markowitz-controlled entity called TMG Limited; in 1981 it obtained tax losses as a customer of TMG Associates; in 1982 Dominion Securities obtained some of its tax losses from an entity known as London & Atlantic Market Brokers Limited. Through the year 1982, Dominion sustained a fictitious loss of approximately $300,000 as a result of its fictitutious trading with London & Atlantic.

20. Defendants Stefanou and Frank were general partners in Dominion Securities, which was organized in December 1980 as a tax shelter, and Dominion Securities was a client of Frank & Co.

21. On or about October 7, 1983 Stefanou prepared, signed and filed a false personal income tax return for 1982, which reported his share of the phony loss from Dominion Securities. Stefanou has admitted that he knew when he filed the return that it was false.

22. The fictitious transactions between London & Atlantic and Dominion Securities continued in 1983. On or about September 1984 Stefanou prepared the 1983 income tax return of Dominion Securities, which included deductions for the sham transactions. Stefanou has admitted that he knew when he prepared the return that it was false.

23. In 1984 Stefanou and Frank & Co. began providing accounting services to a New York partnership

known as Laurel Capital Associates. In 1983 Laurel Capital Associates began obtaining sham tax deductions from phony trading in metals forward contracts with London & Atlantic brokers. In July 1984 Stefanou prepared the 1983 income tax return of Laurel Capital Associates, which included deductions for the sham transactions. Stefanou has admitted that he knew when he prepared the return that it was false.

24. In April 1985 Markowitz pleaded guilty in the United States District Court for the Southern District of New York to having created in excess of $500,000,000 in fictitious tax deductions for investors in various partnerships he organized, including TMG II and TMG Associates.

25. In or about June 1986, Stefanou pleaded guilty in the United States District Court for the Southern District of New York to several counts of tax fraud and aiding and abetting, arising out of the preparation, signing and filing of the income tax return described in paragraphs 21, 22 and 23 of this complaint.

26. Stefanou has admitted that he knew when he prepared the fraudulent tax returns described in paragraphs 21, 22 and 23 herein that claiming sham transactions as deductions on these returns in order to evade taxes was a federal offense.

27. Upon information and belief, Stefanou, prior to November 1981, rendered services as an accountant that did not comply with standards of performance specified by the American Institute of Certified Public Accountants ("AICPA"), and that might, and in fact did, result in a claim being made against Frank & Co. and other defendants.

28. Upon information and belief, Stefanou, prior to November 1981, knew that he had rendered services as an accountant that did not comply with the standards of performance specified by the AICPA and knew of cir-

cumstances which might result in a claim being made against him, Frank & Co. and other defendants herein.

29. Frank & Co. and Stefanou are named as defendants in a lawsuit filed and currently pending in the United States District Court for the District of Columbia entitled *Silverman, et al. v. Weil, et al.*, CA No. 85-2782. The plaintiffs in that lawsuit are or were limited partners in LeHigh Associates, which invested in TMG II, the Markowitz-controlled limited partnership described in paragraphs 15-17 herein. The plaintiffs in the *Silverman* case seek damages from Frank & Co. and Stefanou for losses arising out of LeHigh Associates' investments in TMG II.

THE INSURANCE POLICIES

30. From November 27, 1981 to the present North River has issued three accountants' professional liability policies to Frank & Co., namely Policy No. 23445, Policy No. 38264 and Policy No. 44376. Subject to their other terms, conditions and limitations, the policies provide that North River will pay on behalf of the insured all sums, up to the limits of liability stated in the policies, which the insured becomes legally obligated to pay as damages caused by acts, errors or omissions in the insured's performance of professional accounting services for others, provided that the claim is first made against the insured during the policy period. The policies also provide that, subject to their other terms, conditions and limitations, North River will defend any civil action for damages against the insured, and pay the insured's defense costs.

31. The applications submitted by Frank & Co. for each of the three policies contained the following statement:

> THE UNDERSIGNED BEING AUTHORIZED BY AND ACTING ON BEHALF OF THE APPLI-

CANT AND ALL PERSONS OR CONCERNS SEEKING INSURANCE, HAS READ AND UNDERSTANDS THIS APPLICATION AND DECLARES ALL STATEMENTS SET FORTH HEREIN ARE TRUE, COMPLETE AND ACCURATE. THE UNDERSIGNED FURTHER DECLARES AND REPRESENTS THAT ANY OCCURRENCE OR EVENT TAKING PLACE PRIOR TO THE ISSUANCE OF THE POLICY APPLIED FOR, WHICH MAY RENDER INACCURATE, UNTRUE OR INCOMPLETE ANY STATEMENT MADE HEREIN WILL BE IMMEDIATELY REPORTED IN WRITING TO THE COMPANY. THE UNDERSIGNED ACKNOWLEDGES AND AGREES THAT THE SUBMISSION AND THE COMPANY'S RECEIPT OF SUCH WRITTEN REPORT, PRIOR TO THE INCEPTION OF THE POLICY APPLIED FOR IS A CONDITION PRECEDENT TO COVERAGE.

32. Each of the three policies issued by North River to Frank & Co. contained the following provision:

> By acceptance of this policy, the Insured reaffirms as of the inception date of this policy that (a) the statements in the application attached hereto and made a part hereof are his agreements and representations, (b) that this policy is issued in reliance upon the truth and accuracy of such representations and (c) that this policy embodies all agreements existing between himself and the Company or any of its agents relating to this insurance.

33. The Declaration page of each of the three policies issued by North River to Frank & Co. provided, *inter alia*, that the declarations page, together with the completed and signed application, the accountants' professional liability insurance form, and certain endorsements thereto, constituted the contract between the insured and North River.

34. Defendants Frank & Co., Robert Frank and Peter Stefanou are named insureds under all three of the policies.

35. Defendant J. Miller is a named insured under Policy No. 23445.

36. Defendants Arthur J. Early and Mary Boyle Armstrong are named insureds under Policy No. 38264 and Policy No. 44376.

37. Defendants Hal L. Young, Terry A. Andolshek, Patricia A. Coyle, and Lawrence Goldman are named insureds under Policy No. 44376.

38. Plaintiff has named as defendants herein each of the named insureds under the three policies. If plaintiff later learns that there are additional insureds under any of the policies, plaintiff will seek leave to amend the complaint to include the additional insureds.

Policy No. 23445

39. On or about October 11, 1981, Frank & Co. submitted to North River an application for professional liability insurance, executed by defendant Robert Frank, together with the attachments thereto ("the application for Policy No. 23445").

40. The application for Policy No. 23445, which was received by North River shortly after it was executed by the insured, provided North River with certain critical assurances concerning the nature of the potential risks for which insurance was being sought. For example, the insured represented in its response to question 23 on the application for Policy No. 23445 that, having inquired of all officers, partners and employees, the applicant was unaware of any investigation, inquiries or other circumstances which might result in a claim being made against any applicant, any predecessor in business or any partner(s), officer(s) and employee(s).

41. On or about October 15, 1981, in reliance upon the aforesaid application, North River issued Policy No. 23445 for the period November 27, 1981 through November 27, 1984. The Declarations page of Policy No. 23445 indicated that the limit of liability was $4,000,000.

42. The limit of liability under Policy No. 23445 was increased to $10,000,000 effective March 16, 1982, in reliance upon the insured's representation that it was not aware of any claim or circumstances which might give rise to a claim that had not previously been reported to the insurer.

43. The limit of liability under Policy No. 23445 was increased to $20,000,000 effective November 27, 1982, again in reliance upon the insured's representation that it was not aware of any claim or circumstances which might give rise to a claim that had not previously been reported to the insurer.

Policy No. 38624

44. On or about November 12, 1984, Frank & Company submitted to North River a completed accountant's professional liability insurance application, executed by defendant Peter Stefanou, together with the attachments thereto ("the application for Policy No. 38624").

45. The application for Policy No. 38624 was received by North River shortly after November 12, 1984. Like the application for the previous policy, it provided North River with certain critical assurances concerning the nature of the potential risk for which insurance was being sought. For example, the insured represented in its answer to question 29 that it was unaware of any investigations, inquiries or other circumstances where standards of performance of the AICPA were not complied with.

46. On or about January 16, 1985, in reliance upon the aforesaid application, North River issued and delivered to Frank & Co. Policy No. 38624 for the period November 27, 1984 to November 27, 1987. The Declarations page of Policy No. 38624 indicated that the limit of liability was $20,000,000.

Policy No. 44376

47. On or about September 13, 1985, North River notified Frank & Co. that Policy No. 38624 would be cancelled effective November 27, 1985, due to contractions in the reinsurance market.

48. On or about November 9, 1985, Frank & Co. submitted to North River a completed accountants' professional liability insurance application, executed by defendant Frank Stefanou as a partner of Frank & Co., together with the attachments thereto ("the application for Policy No. 44376").

49. The application for Policy No. 44376 was received by North River shortly after November 9, 1985. As was the case with the applications for the two previous policies, it provided North River with certain critical assurances concerning the nature of the potential risk for which insurance was being sought. For example, the insured represented in its answer to question No. 29 of the application that the insured was unaware of any investigations, inquiries or other circumstances where AICPA standards of performance were not complied with.

50. On or about January 31, 1986, in reliance on the aforesaid application, North River issued and delivered to Frank & Co. Policy No. 44376.

51. The Declarations page of Policy No. 44376 indicated that the limit of liability was $5,000,000.

First Claim for Relief

(Declaratory Relief for Rescission of
Policy No. 23445, Policy No. 38624 and Policy No. 44376)

On information and belief plaintiff alleges as follows:

52. North River repeats and incorporates the allegations of paragraph 1 through 51 herein.

53. The statements in all three of the applications to the effect that Frank & Co. was not aware of any investigations, inquiries, or other circumstances where AICPA standards of performance were not complied with, or of any circumstances that might give rise to a claim, were false.

54. The applications submitted by Frank & Co. to North River did not reveal, among other things: (1) that since late 1980 or early 1981, but in any event prior to November 27, 1981, (the effective date of the earliest policy at issue herein), Frank & Co. had been providing professional accounting services to Edward Markowitz and Markowitz-related entities, and that Frank & Co., Stefanou, and perhaps other defendants as well, were aware that Markowitz's previous accountant had withdrawn from its engagement with Markowitz because it did not believe that there was sufficient evidence that the transactions that generated the tax losses for certain Markowitz-controlled partnerships had ever taken place; (2) that, prior to November 27, 1981, Stefanou, and perhaps other defendants as well, knew that some or all of these partnerships were providing false, fictitious and fraudulent tax deductions; (3) that on or about September 8, 1984 Stefanou knowingly prepared a false 1983 federal income tax return for Dominion Securities, a client of Frank & Co.; (4) that in or about July 1984 Stefanou knowingly prepared a fraudulent 1983 federal income tax return for Laurel Capital Associates, a client of Frank & Co.; and (6) that on or about October 7, 1983,

defendant Stefanou knowingly prepared and filed a false personal income tax return for the year 1982.

55. The representations contained in the applications for the policies, including those set forth in paragraphs 40, 45, and 49 herein were material to the risk to be assumed by North River under the policies.

56. The representations contained in the applications for the policies, including those set forth in paragraphs 40, 45, and 49, were materially false and incomplete. North River relied on the false, material misrepresentations and omissions made in the applications in issuing the policies.

57. The false, material misrepresentations contained in the applications, including those set forth in paragraphs 40, 45, and 49 herein, failed to disclose the actual riks assumed by North River under the policies. Had full, complete and accurate disclosures been made, North River would have known that its risk of loss and exposure to liability would have been substantially greater than the risk that North River was led to believe it assumed under the policies.

58. North River would not have issued the policies in question if truthful and complete information had been furnished to it in the application.

59. An actual dispute exists between North River and the defendants. Several of the insureds are named as defendants in various pending lawsuits, including the one identified in paragraph 25 herein, and North River currently is paying for the defense of these lawsuits on behalf of the insureds. Moreover, certain of the defendants have been advised of other potential claims against them. Defendants allege that such claims against them are covered under one or more of the policies issued to Frank & Co. by North River. North River has expressly reserved its right to deny coverage for these claims and

alleges further that, because the issuance of the policies was induced by material misrepresentations, the policies and each of them is void. North River so notified Frank & Co. of its position on October 6, 1986.

60. As a direct and proximate result of the acts of defendants, North River has suffered substantial loss and damage and may suffer additional substantial loss and damage unless the policies are rescinded.

61. The policies and each of them should be rescinded as void and held of no legal effect under the laws of the state of Virginia. Pursuant to 28 U.S.C. § 2201 *et seq.*, North River seeks a declaratory judgment that the policies are void from their inception and that North River has had, now has, and in the future will have, no obligation to Frank & Co., its partners, employees, or anyone else under the policies.

62. North River is ready, willing and able to tender to Frank & Co. the full amount of the premiums paid by Frank & Co. for the policies in question, plus interest thereon, and has already paid said amount to Frank & Co. for claims submitted under the policies that are void *ab initio*. If this Court determines that fewer than all three policies shall be declared void *ab initio*, or if the amount paid for claims submitted under the policies that are rescinded is less than the amount owed Frank & Co., North River is ready, willing and able to pay any refunded premium to Frank & Co. with interest thereon.

Second Claim for Relief

(Declaratory Relief for Rescission of the Increases in Liability Coverage Under Policy No. 23445)

For and as an alternative cause of action, North River states as follows:

63. North River repeats and incorporates the allegations contained in paragraphs 1 through 58 herein.

64. The representations made in connection with the increases in liability limits under Policy No. 23445 from $4,000,000 to $10,000,000 and from $10,000,000 to $20,000,000 (as set forth in paragraphs 42 and 43 herein) were material to North River's decision to increase the level of liability under that policy.

65. The representations made in connection with the increases in the liability limits were materially false and incomplete. North River relied on these false material misrepresentations and omissions in authorizing the increases in the level of liability under Policy No. 23445. The false material representations made by Frank & Co. in connection with the increases in liability limits failed to disclose the actual risk assumed by North River under the policy. Had full, complete and accurate disclosure been made, North River would have known that its risk of loss and exposure to liability would have been substantially greater than the risk that North River was led to believe it assumed under the policy.

66. North River would not have increased the liability limits under Policy No. 23445 if truthful and complete information had been furnished to it in the representation letters submitted by Frank & Co.

67. If the Court does not issue an order declaring that Policy No. 23445 is void from its inception, then the liability limit increases issued in connection with Policy No. 23445 as of March 16, 1982 and November 27, 1982 should be rescinded, as void, and held of no legal effect under the laws of the state of Virginia. Pursuant to 28 U.S.C. § 2201 *et seq.*, North River seeks a declaratory judgment that these increases in liability limits are void from their inception.

WHEREFORE, North River respectfully prays for judgment in its favor and against defendants, and each of them, and for relief as follows:

1. That this Court declare Policy No. 23445, Policy No. 38624 and Policy No. 44376 void as of their dates of inception and of no force and effect.

2. That this Court declare that North River has no liability whatsoever to any defendant herein or to any other insured under any of the policies.

3. Alternatively, that this Court declare Policy No. 38624 and Policy No. 44376 void as of their dates of inception and of no force and effect and that this Court declare that the increases in the limit of liability under Policy No. 23445 are void and of no effect.

4. That this Court declare that defendants must pay to North River all sums of money paid by North River pursuant to the policies.

5. That North River be awarded its costs and attorneys' fees.

6. Such other and further relief as the Court deems just, necessary and proper.

Respectfully submitted,

/s/ James E. Grossberg
JAMES E. GROSSBERG
1200 S. Courthouse Road, # 330
Arlington, Virginia 22204
(202) 828-4858

By /s/ Wallace A. Christensen
WALLACE A. CHRISTENSEN
MARY HELEN CARLSON
ROSS, DIXON & MASBACK
2000 Pennsylvania Ave., N.W.
Washington D.C. 20006
(202) 828-4800

Attorneys for Plaintiff
North River Insurance Co.

APPENDIX H

UNITED STATES DISTRICT COURT FOR
THE EASTERN DISTRICT OF VIRGINIA
ALEXANDRIA DIVISION

Civil Action No. 86-1173-A

NORTH RIVER INSURANCE COMPANY, INC.,
Plaintiff,

v.

FRANK & COMPANY, P.C., *et al.*,
Defendants.

ANSWER OF DEFENDANTS FRANK & COMPANY, P.C., PETER STEFANOU, ROBERT H. FRANK, HAL L. YOUNG, ARTHUR J. EARLY, MARY BOYLE ARMSTRONG, TERRY A. ANDOLSHEK, PATRICIA A. COYLE and LAWRENCE GOLDMAN

Defendants Frank & Company, P.C., Robert H. Frank, Hal L. Young, Arthur J. Early, Mary Boyle Armstrong, Terry A. Andolshek, Patricia A. Coyle, and Lawrence Goldman (referred to collectively as the "answering defendants"), by their undersigned counsel, answer plaintiff North River Insurance Company's complaint as follows:*

1. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 1.

---

* Defendant Peter Stefanou, upon the advice of counsel, respectfully declines to answer the allegations set forth in plaintiff's complaint on the basis of his constitutional rights.

2. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 2.

3. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 3.

4. The allegations in Paragraph 4 are admitted, except that the answering defendants lack knowledge or information sufficient to form a belief as to North River's state of incorporation and principal place of business.

5. The allegations in Paragraph 5 are admitted.

6. The allegations in Paragraph 6 are admitted, except that the answering defendants deny (a) that Robert H. Frank was a "named insured" under any of the three policies at issue, and (b) that Robert H. Frank resides in and is a citizen of Virginia.

7. The allegations in Paragraph 7 are admitted, except that the answering defendants deny that Peter Stefanou was a "named insured" under any of the three policies at issue.

8. The allegations in Paragraph 8 are admitted, except that the answering defendants deny that Hal L. Young was a "named insured" under any of the three policies at issue.

9. The allegations in Paragraph 9 are admitted, except that the answering defendants deny that Arthur J. Early was a "named insured" under any of the three policies at issue.

10. The allegations in Paragraph 10 are admitted, except that the answering defendants deny that Mary Boyle Armstrong was a "named insured" under any of the three policies at issue.

11. The allegations in Paragraph 11 are admitted, except that the answering defendants deny that Terry A.

Andolshek was a "named insured" under any of the three policies at issue.

12. The allegations in Paragraph 12 are admitted, except that the answering defendants deny that Patricia A. Coyle was a "named insured" under any of the three policies at issue.

13. The allegations in Paragraph 13 are admitted, except that the answering defendants deny that Lawrence Goldman was a "named insured" under any of the three policies at issue.

14. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 14, except that (a) they admit that J. Miller was an employee of Frank & Company during part of the pertinent time period, and (b) they deny that J. Miller was a "named insured" under any of the policies at issue.

15. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 15, except that they admit that in the early 1980s Frank & Company performed some accounting services for Edward Markowitz and various limited partnerships formed and/or controlled by Markowitz.

16. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 16, except that they admit that in the early 1980s Frank & Company performed some accounting services for TMG II.

17. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 17, except that they deny (a) that any defendant knew the reasons for Price-Waterhouse & Co.'s alleged withdrawal, and (b) that Frank & Company or Peter Stefanou prepared the 1980 tax return for TMG II.

18. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 18, except that they admit that Frank & Company performed some accounting serv- for TMG Associates.

19. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 19.

20. The allegations in Paragraph 20 are denied, except that the answering defendants admit that Robert H. Frank and Peter Stefanou were general partners in Dominion Securities Group.

21. The allegations in Paragraph 21 are denied to the extent that the answering defendants lack knowledge or information sufficient to form a belief as to the existence and definition of "phony loss[es]" as that term is used in this Paragraph and as to what precisely Mr. Stefanou knew at the time he filed the return. The answering defendants admit that Mr. Stefanou pled guilty in the Southern District of New York to a violation of 26 U.SC. § 7021.

22. The allegations in Paragraph 22 are denied to the extent that the answering defendants lack knowledge or information sufficient to form a belief as to existence and the definition of "fictitious transactions" and "sham transactions" as those terms are used in this Paragraph and as to precisely what Mr. Stefanou knew at the time the return was prepared. The answering defendants admit that Mr. Stefanou pled guilty in the Southern District of New York to a violation of 26 U.S.C. § 7206(2) in connection with the preparation of this return.

23. The allegations in Paragraph 23 are denied to the extent that the answering defendants lack knowledge or information sufficient to form a belief as to the existence and definition of "sham tax deductions," "sham transactions," and "phony trading in metals" as those terms are

used in this Paragraph and as to precisely what Mr. Stefanou knew at the time the return was prepared. The answering defendants admit that Mr. Stefanou pled guilty in the Southern District of New York to a violation of 26 U.S.C. § 7206(2) in connection with the preparation of this return.

24. The allegations in Paragraph 24 are admitted, except that the answering defendants lack knowledge or information sufficient to form a belief as to the existence and definition of "fictitious tax deductions" as used in this Paragraph and the amount of such deductions.

25. The allegations in Paragraph 25 are admitted, but only to the extent that Mr. Stefanou pled guilty to one count of violating 26 U.S.C. § 7201 and two counts of violating 26 U.S.C. § 7206(2).

26. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 26, except that Mr. Stefanou pled guilty in the Southern District of New York to violations of 26 U.S.C. §§ 7201 and 7206(2).

27. The allegations in Paragraph 27 are denied.

28. The allegations in Paragraph 28 are denied.

29. The allegations in Paragraph 29 are admitted, except that the name of the partnership is "Lehigh," not "LeHigh." The plaintiffs' suit against Frank & Company and Stefanou was dismissed in December 1986 for the third time and has just been refiled.

30. The allegations in Paragraph 30 are admitted, except that the answering defendants deny that any of the policies bore the number "38264."

31. The allegations in Paragraph 31 are admitted.

32. The allegations in Paragraph 32 are admitted.

33. The allegations in Paragraph 33 are admitted.

34. The allegations in Paragraph 34 are denied.

35. The allegation in Paragraph 35 is denied.

36. The allegations in Paragraph 36 are denied.

37. The allegations in Paragraph 37 are denied.

38. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 38, except that they admit that the named insured under each of the three policies at issue has been named as a defendant in this suit.

39. The allegations in Paragraph 39 are admitted.

40. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 40, except that they admit that the application for Policy No. 23445 contained the following question, to which Frank & Company answered in the negative: "Having inquired of all officers, partners, and employees, is the Applicant aware of any investigation, inquiries or other circumstances which may result in a claim being made against Applicant, any predecessor in business or any partner(s), officer(s), or employees(s)?"

41. The allegations in Paragraph 41 are admitted, except that the answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegation that North River issued Policy No. 23445 in reliance upon Frank & Company's application.

42. The allegations in Paragraph 42 are denied, except that the answering defendants admit that the limit of liability under Policy No. 23445 was increased to $10,000,000 effective March 16, 1982.

43. The allegations in Paragraph 43 are denied, except that the answering defendants admit that the limit of liability under Policy No. 23445 was increased to $20,000,000 effective November 27, 1982.

44. The allegations in Paragraph 44 are admitted.

45. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 45, except that they admit that Frank & Company represented on its application for Policy No. 38624 that it was unaware of any investigations, inquiries or other circumstances where AICPA standards of performance were not complied with.

46. The allegations in Paragraph 46 are admitted, except that the answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegation that North River issued Policy No. 38624 in reliance on Frank & Company's application.

47. The allegations in Paragraph 47 are admitted.

48. The allegations in Paragraph 48 are admitted, except that the answering defendants deny that the application submitted by Frank & Company on or about November 9, 1985 was executed by Frank Stefanou.

49. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 49, except that they admit that Frank & Company represented on its application for Policy No. 44376 that it was unaware of any investigations, inquiries or other circumstances where AICPA standards of performance were not complied with.

50. The allegations in Paragraph 50 are admitted, except that the answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegation that North River issued Policy No. 44376 in reliance on Frank & Company's application.

51. The allegation in Paragraph 51 is admitted.

52. The answering defendants repeat and incorporate their responses to the allegations in Paragraphs 1 through 51 as their answer to Paragraph 52.

53. The allegations in Paragraph 53 are denied.

54. The answering defendants admit that Frank & Company's three applications did not mention the matters alleged in Paragraph 54. To the extent that the numbered clauses are construed to be allegations, the answering defendants admit the allegations in the clauses numbered (3), (4), and (6), except that they deny that Dominion Securities was a client of Frank & Company, and they lack knowledge or information sufficient to define the term "knowingly" as used in these clauses and to know what Mr. Stefanou actually knew at that time. The answering defendants admit that Mr. Stefanou pled guilty in the Southern District of New York to violations of 26 U.S.C. §§ 7201 and 7206(2). In all other respects the allegations in Paragraph 54 are denied.

55. The allegations in Paragraph 55 are denied.

56. The allegations in Paragraph 56 are denied.

57. The allegations in Paragraph 57 are denied.

58. The allegations in Paragraph 58 are denied.

59. The answering defendants lack knowledge or information sufficient to form a belief as to the truth of the allegations in Paragraph 59, except that the insureds are defendants in only two lawsuits, one relating to matters alleged in the plaintiff's complaint and one totally unrelated to matters alleged in plaintiff's complaint.

60. The allegations in Paargraph 60 are denied.

61. The answering defendants deny that North River is entitled to the relief it seeks in Paragraph 61.

62. The allegations in Paragraph 62 are admitted, except that the only amounts paid out by plaintiff to the insureds relate to plaintiff's obligation to defend the insured. No amounts have ever been paid out by the plaintiff-insurer to the insured by virtue of any verdict

or judgment against the insured or any settlement entered into by the insured.

63. The answering defendants repeat and incorporate their responses to the allegations in Paragraphs 1 through 58 as their answer to Paragraph 63.

64. The allegations in Paragraph 64 are denied.

65. The allegations in Paragraph 65 are denied.

66. The allegations in Paragraph 66 are denied.

67. The answering defendants deny that North River is entitled to any of the relief that it seeks.

FIRST AFFIRMATIVE DEFENSE: ESTOPPEL

68. In a series of letters beginning March 13, 1984, Frank & Company, through counsel, informed L.W. Biegler, Inc., a representative of North River Insurance Company ("North River"), that certain work Frank & Company had done for Edward Markowitz and entities that he controlled could give rise to claims for damages against Frank & Company.

69. As of March 13, 1984, North River had knowledge of facts sufficient to put a reasonably prudent person on notice of the possibility that Frank & Company had made misrepresentations on its applications for Policy No. AL-23445 and the increases in coverage dated March 16, 1982 and November 27, 1982.

70. Notwithstanding its notice of Frank & Company's possible misrepresentation on the application for Policy No. AL-23445, North River (a) issued Policy No. AL-38624 to Frank & Company on or about January 16, 1985, effective November 27, 1984, to November 27, 1987; (b) issued Policy No. AL-44376 to Frank & Company on or about January 31, 1986, effective November 25, 1985, to November 25, 1986; (c) requested and received information from Frank & Company concerning the Mar-

kowitz matter and other claims and potential claims against Frank & Company; and (d) supervised Frank & Company's defense in *Silverman et al. v. Weil et al.*, Civ. No. 85-2782 (D.D.C.) and *46th Street Associates Limited Partnership v. Frank, Stefanou & Co.*, No. 69804 (19th Cir. Ct. Fairfax County, Va.).

71. North River's conduct in (a) renewing Frank & Company's insurance coverage twice; (b) requesting and receiving information from Frank & Company concerning the Markowitz matter and other claims and potential claims; and (c) supervising Frank & Company's defense in the *Silverman* and *46th Street Associates* actions, caused Frank & Company to believe until October 6, 1986 (the day North River filed this action) that North River had a subsisting contractual obligation to insure Frank & Company against professional malpractice claims and to defend such claims on Frank & Company's behalf.

72. Frank & Company, acting in reliance on North River's conduct and to its own prejudice, (a) did not attempt to obtain insurance with another insurer at any time between March 13, 1984 and October 6, 1986; (b) provided North River with confidential information concerning the Markowitz matter; and (c) consented to North River's supervision of Frank & Company's defense in the *Silverman* and *46th Street Associates* actions.

73. Because Frank & Company relied prejudicially on North River's conduct, North River is estopped from rescinding Policies AL-23445, AL-38624, and AL-44376.

SECOND AFFIRMATIVE DEFENSE: WAIVER

74. The allegations in ¶¶ 68-73 above are incorporated herein by reference.

75. Through its conduct, North River has waived its right, if any, to rescind Policies AL-23445, AL-38624, and AL-44376.

THIRD AFFIRMATIVE DEFENSE:
LACHES AND STATUTE OF LIMITATIONS

76. North River's action is barred by laches and by the applicable statute of limitations.

Respectfully submitted,

WILLIAMS & CONNOLLY

By: /s/ John D. Cline
TERRENCE O'DONNELL
JOHN D. CLINE
839 17th Street, N.W.
Washington, D.C. 20006
(202) 331-5504

MICHAEL MCGETTIGAN
921 King Street
Alexandria, Virginia 22314
(703) 549-5353

Attorneys for Defendants
Frank & Company, P.C.,
Peter Stefanou,
Robert H. Frank,
Hal L. Young,
Arthur H. Early,
Mary Boyle Armstrong,
Terry A. Andolshek,
Patricia A. Coyle,
Lawrence Goldman

Dated: January 6, 1987

JURY DEMAND

Defendants demand a trial by jury.

MICHAEL MCGETTIGAN

CERTIFICATE OF SERVICE

I hereby certify that on January 6, 1987, a true copy of the foregoing Answer of Defendants Frank & Company, P.C., Peter Stefanou, Robert H. Frank, Hal L. Young, Arthur J. Early, Mary Boyle Armstrong, Terry A. Andolshek, Patricia A. Coyle, and Lawrence Goldman was hand-delivered to James E. Grossberg, counsel for plaintiff North River Insurance Company, Inc., at the following address: 1200 S. Courthouse Road, #330, Arlington, Virginia 22204.

/s/ John D. Cline
JOHN D. CLINE

Supreme Court, U.S.
FILED
APR 19 1988
JOSEPH F. SPANIOL, JR.

No. 87-1552

IN THE
Supreme Court of the United States
OCTOBER TERM, 1987

PETER STEFANOU,
Petitioner,

v.

NORTH RIVER INSURANCE COMPANY, INC.,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

---

BRIEF FOR THE RESPONDENT IN OPPOSITION

WALLACE A. CHRISTENSEN
Counsel of Record
MARY HELEN CARLSON
ROSS, DIXON & MASBACK
555 13th Street, N.W.
Washington, D.C. 20004-1109
(202) 662-2000
Attorneys for Respondent North River Insurance Company

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

QUESTION PRESENTED

Whether judgment on the pleadings may be entered against a civil defendant who refuses to answer any of the allegations of the complaint on the basis of his Fifth Amendment rights, where (a) it is undisputed that answers to the vast majority of the allegations pose no danger of incrimination; and (b) even after a court ruling that the claim of privilege was improperly invoked, the defendant fails to move to amend his answer so as to respond to those allegations that pose no danger of incrimination.

RULE 28.1 LIST

Respondent North River Insurance Company is a wholly-owned subsidiary of Crum and Forster, Inc. Crum and Forster is a wholly-owned subsidiary of Xerox Financial Services, Inc., which is a wholly-owned subsidiary of Xerox Corporation.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
RULE 28.1 LIST	ii
TABLE OF AUTHORITIES	iv
OPINIONS BELOW	1
JURISDICTION	2
CONSTITUTIONAL PROVISION INVOLVED	2
RULE OF CIVIL PROCEDURE INVOLVED	2
STATEMENT OF THE CASE	2
ARGUMENT	5
1. The Court Of Appeals' Decision Is Correct And Fair	5
2. There Is No Conflict Between The Fourth Circuit's Decision And Any Decision Of This Court Or Any Court Of Appeals	9
CONCLUSION	12

TABLE OF AUTHORITIES

Cases: Page

Anglada v. Sprague, 822 F.2d 1035 (11th Cir. 1987) 6
Davis v. Fendler, 650 F.2d 1154 (9th Cir. 1981) 6
Garner v. United States, 424 U.S. 648 (1976) 6, 7
General Dynamics Corp. v. Selb Manufacturing Co., 481 F.2d 1204 (8th Cir. 1973), *cert. denied*, 414 U.S. 1162 (1974) 6
Hoffman v. United States, 341 U.S. 479 (1951) 7, 8
Maness v. Meyers, 419 U.S. 449 (1975) 7
Mills v. United States, 281 F.2d 736 (4th Cir. 1960) 9
National Acceptance Co. of America v. Bathalter, 705 F.2d 924 (7th Cir. 1983) 9, 10, 11
Rogers v. Webster, 776 F.2d 607 (6th Cir. 1985) 9, 10, 11
United States v. Carroll, 567 F.2d 955 (10th Cir. 1977) 6
United States v. Grabinski, 558 F. Supp. 1324 (D. Minn. 1983), *modified*, 727 F.2d 681 (8th Cir. 1984) 6
United States v. Murdock, 290 U.S. 389 (1933) 6
United States v. Yurasovich, 580 F.2d 1212 (3d Cir. 1978) 7
Washington v. Yakima Indian Nation, 439 U.S. 463 (1979) 11

Statutes and Rules:

26 U.S.C. § 7203 (1982) 6, 7
28 U.S.C. § 1254(1) (1982) 2
Fed. R. Civ. P. 8(d) ..... *passim*

Secondary Authorities:

5 C. Wright & A. Miller, *Federal Practice & Procedure* § 1280 (1969) 6

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

No. 87-1552

PETER STEFANOU,

Petitioner,

v.

NORTH RIVER INSURANCE COMPANY, INC.,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

---

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals is reported at 831 F.2d 484 and is reprinted at App. 1a-7a.[1] The district court's unreported order is reprinted at App. 23a-24a, and its unreported oral opinion is reprinted at App. 8a-21a.

---

[1] In keeping with the method used in the petition, references herein to "App." are to the Appendix to the petition. References to "C.A." are to the Joint Appendix filed in the Court of Appeals. References to "Pet." are to the petition itself. References to "¶" are to the paragraphs of the complaint in this case, which is included in the Appendix to the petition at pages 28a-44a.

JURISDICTION

The judgment of the court of appeals was entered on October 16, 1987. App. 26a. A timely petition for rehearing, with a suggestion for rehearing en banc, was denied on December 21, 1987. App. 27a. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISION INVOLVED

The Fifth Amendment to the United States Constitution provides in pertinent part:

> No person . . . shall be compelled in any criminal case to be a witness against himself. . . .

RULE OF CIVIL PROCEDURE INVOLVED

Rule 8(d) of the Federal Rules of Civil Procedure provides in pertinent part:

> Averments in a pleading to which a responsive pleading is required, other than those as to the amount of damage, are admitted when not denied in the responsive pleading.

STATEMENT OF THE CASE

Beginning in November 1981, respondent North River Insurance Company ("North River") issued a series of accountants' professional liability insurance policies to the accounting firm of Frank & Co., P.C. and a number of its partners and employees, including petitioner Peter Stefanou ("Stefanou"). App. 35a, 49a. In issuing the policies, North River relied on applications representing that Stefanou had no knowledge of facts or circumstances that might give rise to a claim. App. 37a-39a. After the policies issued, Stefanou pled guilty to three criminal tax offenses, and was sued for involvement in a tax fraud scheme dating back to 1980. App. 2a, 35a, 49a. That scheme was masterminded by one Edward Marko-

witz, who pled guilty to creating over $500,000,000 in false tax deductions for investors in various partnerships and limited partnerships he had organized. Stefanou had provided accounting services to Markowitz and Markowitz-related entities. App. 2a, 31a-34a, 48a-49a; C.A. 65-66, 119. As part of his plea bargain, Stefanou was granted immunity from prosecution for certain criminal violations, including criminal tax violations, arising from his involvement with 40 named companies, including many Markowitz-related ones. App. 3a; C.A. 50-54.

Upon learning of Stefanou's plea, North River sued him and the other insureds for rescission of the policies, on the ground that the policy applications contained material misrepresentations of fact concerning the insureds' knowledge of facts and circumstances likely to give rise to a claim. App. 2a, 28a-44a. Stefanou refused to answer *any* of the allegations of the complaint, simply stating in a footnote to the other defendants' answer that:

> Defendant Peter Stefanou, upon the advice of counsel, respectfully declines to answer the allegations set forth in plaintiff's complaint on the basis of his constitutional rights.

App. 45a. Stefanou made this blanket refusal to answer the complaint even though responses to the vast majority of the allegations could, under no circumstances, be deemed incriminating.[2]

---

[2] For example, Stefanou refused to answer allegations concerning jurisdiction and venue (¶¶ 1-3), the identity of the parties (¶¶ 4-14), the existence of a civil suit against him (¶ 29), the terms of and facts about the insurance policies in question (¶¶ 30-51), the materiality of the representations in the policy applications (¶¶ 55, 64), the existence of a dispute among the parties (¶ 59), the nature of relief being sought (¶¶ 61, 67) and North River's willingness to return the premiums paid for the policies (¶ 62). App. 3a, 29a-44a. Nor would Stefanou admit or deny that he had pled guilty to several counts of tax fraud (¶ 25), even though his plea was made in open court and is a matter of public record. App. 3a.

For the same reason and in the same manner, Stefanou refused to respond to a request for admissions filed by North River, even though he had failed to make any objection to the requests within the time required by local rule. C.A. 175.

North River moved for judgment on the pleadings, contending that Stefanou's blanket invocation of the Fifth Amendment was improper and thus his failure to deny the allegations of the complaint constituted an admission of those allegations under Fed. R. Civ. P. 8(d). App. 3a; C.A. 68-77. North River also moved to have its requests for admissions deemed admitted on the basis of Stefanou's improper and untimely objections to the requests.

The district court granted the motion for judgment on the pleadings against Stefanou on the ground that Stefanou's indiscriminate claim of privilege did not allow the court to determine whether "there had been some consideration of each allegation as to whether it would [incriminate him] or not." App. 17a. In its written order, the district court confirmed that "the attempted invocation by the defendant Peter Stefanou of his Fifth Amendment right not to answer the allegation [sic] of the complaint was ineffective and improperly done." App. 23a. North River's motion to deem its requests for admissions admitted likewise was granted by a magistrate. C.A. 155. The district court thereafter denied motions to reconsider each of the orders. App. 25a; C.A. 197. At no time did Stefanou file a motion for leave to amend his answer, even after the district court ruled that his blanket invocation of the Fifth Amendment was improper.

On appeal, the Fourth Circuit affirmed the district court's order granting judgment on the pleadings. The court of appeals acknowledged that, when properly invoked, the privilege against self-incrimination can avoid the operation of Rule 8(d), but noted that "the mere

'blanket refusal to answer questions does not suffice to raise constitutional questions.'" App. 4a (citations omitted). A proper invocation of the Fifth Amendment, the court ruled, requires the defendant to "answer those allegations that he can and to make a specific claim of privilege as to the rest." *Id.* Only then is "an informed ruling on the claim" possible. App. 5a. "Under the circumstances of this case," the court held that Stefanou's "blanket refusal to answer or respond was not sufficient." *Id.*

The Fourth Circuit rejected Stefanou's argument that it was the district court's responsibility to "pierce his blanket assertion of privilege to determine its merits" as to each allegation of the complaint. Rather, the court stated, a party seeking to make a good faith assertion of the privilege must do so with sufficient particularity to allow an informed ruling on the claim. *Id.* The court found that Stefanou could have answered many of the allegations of the complaint without fear of incrimination. "Instead, he chose a course of action which left the district court with no reasonable alternative other than to enter judgment against him." App. 6a (citation omitted).

The court also rejected Stefanou's alternative argument that the case should be remanded to the district court with instructions to allow him to amend his answer. It declined to consider that argument on appeal, because Stefanou had not filed a motion for leave to amend his answer in the district court. App. 6a.

ARGUMENT

The Court should deny the petition because (1) the court of appeals' decision is correct and fair, and (2) there is no conflict between the court of appeals' decision and any decision of this Court or any court of appeals.

1. *The Court of Appeals' Decision Is Correct And Fair.*

The Fourth Circuit's decision that only the *proper* invocation of the privilege against self-incrimination can

avoid the operation of Rule 8(d) is correct and in accord with settled law. App. 4a. *See, e.g.*, 5 C. Wright & A. Miller, *Federal Practice & Procedure* § 1280 at 360 (1969); *Davis v. Fendler*, 650 F.2d 1154, 1159-60 (9th Cir. 1981). The party claiming the privilege is required "to answer those allegations he can and make a specific claim of privilege as to the rest." 5 C. Wright & A. Miller, *Federal Practice & Procedure* § 1280 at 360. *See General Dynamics Corp. v. Selb Mfg. Co.*, 481 F.2d 1204, 1212 (8th Cir. 1973), *cert. denied*, 414 U.S. 1162 (1974) (privilege must be asserted with respect to particular allegations). The mere "blanket refusal to answer questions does not suffice to raise constitutional questions," *United States v. Carroll*, 567 F.2d 955, 957 (10th Cir. 1977), because "it forces the reviewing court to speculate as to which questions would tend to incriminate." *Anglada v. Sprague*, 822 F.2d 1035, 1037 (11th Cir. 1987).

The cases cited by Stefanou in Section I of his petition are readily distinguishable. Each of them addresses a situation in which the assertion of the privilege may result in the imposition of sanctions for willful, criminal conduct. None of petitioner's cases involves the operation of Fed. R. Civ. P. 8(d), which, by contrast, does not depend on the intent of the pleader. Nor is any such criminal sanction involved here.[3]

---

[3] Several cases cited by Stefanou, *e.g.*, *Garner v. United States*, 424 U.S. 648 (1976), *United States v. Murdock*, 290 U.S. 389 (1933), and *United States v. Grabinski*, 558 F. Supp. 1324 (D. Minn. 1983), *modified on other grounds*, 727 F.2d 681 (8th Cir. 1984), involved prosecutions under 26 U.S.C. § 7203 (or identical predecessor statutes) against taxpayers who improperly asserted the Fifth Amendment on their tax returns. Since § 7203 explicitly states that only a willful failure to file a return is a violation of the statute, a defendant could not properly be convicted for an erroneous claim of Fifth Amendment privilege asserted in good faith. Consequently, this Court noted that the protection afforded by § 7203 is broader than the protection provided by the Fifth

In addition, Stefanou's reliance on *Maness v. Meyers*, 419 U.S. 449 (1975), and *Hoffman v. United States*, 341 U.S. 479 (1951), simply ignores the distinction between the "threshold" issue of whether the Fifth Amendment was validly invoked so as to raise a constitutional question, and the quite different and subsequent issue of the consequences of an effective and proper, but possibly erroneous, assertion of the Fifth Amendment. The cases relied on by petitioner address the latter issue, while it is the former issue that is presented in this case. *See, e.g., United States v. Yurasovich*, 580 F.2d 1221 (3rd Cir. 1978) (court must determine whether, as to a particular question, the answer sought might be incriminating, only after a "prima facie claim of privilege is raised," citing *Maness* and *Hoffman*).

Moreover, the Fourth Circuit's decision does not raise the broad questions articulated by Stefanou in his petition. The opinion is not a sweeping pronouncement that a defendant who properly asserts a claim of privilege can have judgment entered against him if a court later determines that a response to a particular inquiry would not be incriminating. Rather, the court of appeals simply decided that "*under the circumstances of this case*" (emphasis added) the Fifth Amendment privilege was not validly invoked in the first instance, and

---

Amendment. 424 U.S. at 663. The Court also noted that in situations other than a § 7203 prosecution, a mere erroneous assertion of the privilege warrants a sanction. 424 U.S. at 663 n.18, citing *Maness v. Meyers*, 419 U.S. 449, 460-61 (1975).

Finally, the Court expressly rejected the contention that the Fifth Amendment guarantee requires a preliminary procedure for testing the validity of an asserted privilege before a defendant can be sanctioned for erroneously claiming the privilege: "The Court previously has considered Fifth Amendment claims in the context of a criminal prosecution where the defendant did not have the benefit of a preliminary judicial ruling on a claim of privilege. It has never intimated that such a procedure is other than permissible." 424 U.S. at 664.

was therefore insufficient to avoid the operation of Fed. R. Civ. P. 8(d). The "circumstances of this case" reflect an exercise in procedural gamesmanship by Stefanou. After twice requesting and obtaining additional time to file an answer, Stefanou then simply refused to respond to anything in the complaint. He made no attempt whatsoever to distinguish between the relatively few allegations calling for answers that might be incriminating, and the vast majority of those calling for answers that unquestionably could not incriminate him.[4]

The "circumstances of this case" also include the simple fact that Stefanou never once moved for leave to file an amended answer, even after the district court ruled that his blanket assertion of a claim of privilege was improper. Consequently, the suggestion in Stefanou's petition that this case involves a situation in which "the defendant is not permitted to replead" (Pet. (i)) is simply wrong. Whether Stefanou should have been permitted to replead is not, and has never been, an issue in the case. Since Stefanou did not request the opportunity to replead in the district court, the Fourth Circuit properly noted that that issue would not be addressed on appeal.[5]

---

[4] As noted previously, Stefanou refused to answer such obviously nonincriminating allegations as those relating to diversity jurisdiction and venue, the fact that North River is an insurance company, and the fact that Stefanou applied for and obtained an insurance policy from North River. Stefanou also refused to admit or deny that he pled guilty to several counts of tax fraud, even though his plea was made in open court and is a matter of public record. The situation here contrasts sharply with that in *Hoffman v. United States*, 341 U.S. 479 (1951), where this Court reversed a criminal contempt conviction based upon a witness's refusal to answer questions. In *Hoffman*, every one of the questions that the defendant refused to answer "could easily have required answers that would forge links in the chain of facts imperiling petitioner with conviction of a federal crime." 341 U.S. at 488.

[5] Petitioner contends that he had no opportunity to reconsider his assertion of the privilege. Pet. 4-6, 8. To the contrary, he had

Finally, the court of appeals' decision has not "ignored settled law in this Circuit," as the dissent suggests. App. 7a. The "settled law" cited by the dissent does not address the issues in this case. *Mills v. United States*, 281 F.2d 736 (4th Cir. 1960), stands for the proposition that there is no "ritualistic formula or talismanic phrase" required to invoke the Fifth Amendment privilege, so long as the court reasonably understands that the speaker is attempting to invoke the privilege. 281 F.2d at 740, 741 (citations omitted). However, the fact that Stefanou referred to his "Constitutional rights" rather than "the Fifth Amendment," or that he did so in a footnote rather than the text, has never been the issue in this case, and it certainly is not raised by the petition. Rather, it is the dozens of allegations that Stefanou could have answered but did not, that made his invocation of the privilege improper. *See* App. 3a-6a. To the extent that *Mills* addresses that issue, *see* 281 F.2d at 740-41, it supports the majority's opinion, in that the only two questions the witness in *Mills* refused to answer were obviously incriminating.

2. ***There Is No Conflict Between The Fourth Circuit's Decision And Any Decision Of This Court Or Any Court Of Appeals.***

Contrary to petitioner's assertion, there is no conflict between the decision below and *Rogers v. Webster*, 776 F.2d 607 (6th Cir. 1985), or *National Acceptance Co. of America v. Bathalter*, 705 F.2d 924 (7th Cir. 1983). These decisions are distinguishable from the decision

---

every opportunity to seek leave to amend his pleadings, but, as the court of appeals found, he simply "did not seek to amend or otherwise alter his position." App. 3a. Stefanou twice (once in his opposition to the motion for judgment on the pleadings and once in his motion for reconsideration) said that he would seek leave to amend if the court ruled against him. C.A. 93, 146-47. He never did so, however. Having made the tactical decision not to file a motion to amend, petitioner cannot now fairly argue that he was not permitted to replead.

below in several significant respects. Neither *Rogers* nor *Bathalter* considered, much less decided, whether a blanket refusal to respond to all averments in a pleading constituted a proper or valid assertion of the Fifth Amendment privilege. Those cases simply held that a *proper* or *valid* invocation of the privilege in response to specific allegations precludes a determination that the allegations are admitted.[6] Consequently, the Fourth Circuit properly determined that neither of those cases was "dispositive of the issue presented here" since "neither case dealt with the threshold issue of whether the Fifth Amendment privilege has been properly asserted so as to allow the district court to make a reasonable assessment of the risk of incrimination." App. 4a.

Unlike North River, which expressly challenged Stefanou's blanket assertion of privilege before the district court, the plaintiffs in *Bathalter* and *Rogers* never raised that threshold issue. Accordingly, in *Bathalter*, the Seventh Circuit ruled that the district court correctly had assumed it could not compel the defendant to respond to the complaint, because the plaintiff "did not take issue with the propriety of claiming the privilege." 705 F.2d at 927. Likewise, there is no suggestion in *Rogers* that the plaintiff in that case ever challenged the nature of the defendant's invocation of the privilege. Indeed, although the Sixth Circuit disapproved of the defendant's blanket assertion of the privilege, it noted that the district court had not addressed the issue. 776 F.2d at 611 n.4.

Moreover, *Rogers* and *Bathalter* can be distinguished from this case on the further ground that neither of those cases involved an indiscriminate refusal to respond

---

[6] The Fourth Circuit does not take a different position. "[W]hen properly invoked, the fifth amendment privilege against self-incrimination, which applies to civil proceedings as well as criminal, can avoid the operation of Rule 8(d)." App. 3a-4a.

to clearly nonincriminating allegations. In *Bathalter*, the Seventh Circuit noted that "[t]he allegations of the complaint are such that an affirmative answer to almost any one of them would provide either direct evidence of criminality or 'a link in the chain of evidence needed to prosecute.'" 705 F.2d at 927 n.5 (citations omitted).

Similarly, in *Rogers*, the defendant refused to comply with two orders of the district court, and the plaintiff moved to have him held in both civil and criminal contempt. *See* 776 F.2d at 607. In lieu of answering the specific averments against him or filing counter-affidavits, the defendant invoked his privilege against self-incrimination. *Id.* at 611. Because the same conduct formed the basis of the civil and criminal proceedings against him, any answer to the civil charges would have applied equally to the criminal charges and, therefore, posed a threat of incrimination.

Two courts have correctly resolved the issues presented by this case. There is no conflict between the decision below and any decision of this Court or any court of appeals. Further review therefore is not warranted.[7]

---

[7] In the alternative, the judgment of the court below can be defended on the ground that Stefanou failed to interpose timely objections to dispositive requests for admissions filed by North River. (Stefanou has conceded that a ruling in North River's favor on its requests for admissions "would deem all essential elements of its case admitted." C.A. 101.) The issue was raised and briefed in both the district court and the court of appeals, but not ruled on by either court. App. 7a. A prevailing party can "defend its judgment on any ground properly raised below whether or not that ground was relied upon, rejected, or even considered by the District Court or the Court of Appeals." *Washington v. Yakima Indian Nation*, 439 U.S. 463, 476 n.20 (1979).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

WALLACE A. CHRISTENSEN
Counsel of Record
MARY HELEN CARLSON
ROSS, DIXON & MASBACK
555 13th Street, N.W.
Washington, D.C. 20004-1109
(202) 662-2000
Attorneys for Respondent
North River Insurance
Company

April 18, 1988

Supreme Court, U.S.
FILED
APR 21 1988
JOSEPH F. SPANIOL, JR.
CLERK

No. 87-1552

IN THE
Supreme Court of the United States
OCTOBER TERM, 1987

PETER STEFANOU,
Petitioner,

v.

NORTH RIVER INSURANCE COMPANY, INC.,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

---

PETITIONER'S REPLY BRIEF

PETER J. KAHN
Counsel of Record
TERRENCE O'DONNELL
JOHN D. CLINE
WILLIAMS & CONNOLLY
839 17th Street, N.W.
Washington, D.C. 20006
(202) 331-5000
Attorneys for Petitioner Peter Stefanou

April 21, 1988

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	i
ARGUMENT	1
CONCLUSION	4

TABLE OF AUTHORITIES

Cases:

Garner v. *United States*, 424 U.S. 648 (1976)	1, 2
Hoffman v. *United States*, 341 U.S. 479 (1951)	2
National Acceptance Co. v. *Bathalter*, 705 F.2d 924 (7th Cir. 1983)	3
Rogers v. *Webster*, 776 F.2d 607 (6th Cir. 1985)	3

Constitutional Provisions:

U.S. Const. amend. V ..... *passim*

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

No. 87-1552

PETER STEFANOU,

Petitioner,

v.

NORTH RIVER INSURANCE COMPANY, INC.,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

---

PETITIONER'S REPLY BRIEF

In its Brief in Opposition ("Opp."), North River makes no claim that Stefanou acted in bad faith in asserting his Fifth Amendment privilege in response to North River's complaint. And North River does not deny that answers to the key substantive allegations in its complaint could have tended to incriminate Stefanou.[1] On this much the parties appear to agree.

In other respects, however, North River's brief is wide of the mark. North River misses the point in arguing that *Garner* v. *United States*, 424 U.S. 648 (1976), can

---

[1] Significantly, North River's list of assertedly unincriminating allegations does not include any of the crucial allegations concerning Stefanou's alleged dealings with Markowitz that formed the heart of North River's complaint. Opp. 3 n.2; App. 31a-34a, 40a-41a.

be distinguished because it involved a criminal prosecution where willfulness was an essential element of the offense. Opp. 6 & n.3. The Court should grant certiorari precisely *because* it left open in *Garner* the significant issue that this case presents: whether a civil defendant who invokes the privilege too broadly in good faith may have judgment rendered against him without an opportunity to replead.

North River errs in citing *Garner* for the proposition that "in situations other than a § 7203 prosecution, a mere erroneous assertion of the privilege warrants a sanction." Opp. 7 n.3 (citing *Garner*, 424 U.S. at 663 n.18). *Garner* noted that "a witness who risks contempt to challenge a judicial order to disclose" faces an immediate sanction if his challenge is unsuccessful. 424 U.S. at 663 n.18. As *Garner* pointed out, however, the witness who asserts the privilege "receives a judicial ruling at that time on the validity of his claim, *and he has an opportunity to reconsider it before being held in contempt for refusal to answer.*" *Id.* at 663 (emphasis added).

The district court entered judgment against Stefanou without a finding of willfulness or bad faith, and without providing him "a judicial ruling [and] an opportunity to reconsider" his assertion of privilege. Thus, Stefanou did not receive the protection afforded either to the taxpayer who asserts the privilege in good faith on his tax return, or to the witness who asserts the privilege in court. Whether a civil defendant may be penalized for invoking the privilege too broadly without *either* a showing of bad faith *or* an opportunity to replead is the question this Court should grant certiorari to decide.

North River emphasizes repeatedly that Stefanou did not formally move to amend his answer after the district court had entered judgment against him. Opp. 4, 5, 8, 9 n.5. But Stefanou did not move to amend because the district court—contrary to its duty under *Hoffman* v. *United States*, 341 U.S. 479, 486 (1951)—refused to rule

as to which of North River's allegations could tend to incriminate Stefanou and which could not.

Rather than moving to amend without knowing what the amendment would entail, Stefanou declared to the district court that he "stands ready to amend his Answer, invoking the privilege where the Court deems appropriate and responding where the Court finds (1) that the response could not possibly tend to incriminate him, and (2) that the response would not waive Mr. Stefanou's privilege." C.A. 146. The district court never made the requested ruling, and Stefanou was therefore unable to amend. Contrary to North River's assertion, Opp. 8, "[w]hether Stefanou should have been permitted to replead" clearly *is* an issue before this Court, as it was before the district court and the court of appeals.

Finally, North River's attempt to distinguish *Rogers* v. *Webster*, 776 F.2d 607 (6th Cir. 1985), and *National Acceptance Co.* v. *Bathalter*, 705 F.2d 924 (7th Cir. 1983), Opp. 9-11, simply ignores the key language in those opinions. As Stefanou pointed out in his Petition, Pet. 10, both cases approved methods of asserting the Fifth Amendment privilege virtually identical to Stefanou's. *See Rogers*, 776 F.2d at 611 n.4; *Bathalter*, 705 F.2d at 927 n.5. The decisions of the Sixth and Seventh Circuits conflict squarely with the decision of the Fourth Circuit below.[2]

---

[2] North River's claim that the judgment of the court of appeals can be upheld on the basis of Stefanou's allegedly untimely assertion of the privilege in response to North River's requests for admissions, Opp. 11 n.7, borders on the frivolous. The magistrate below deemed the requests admitted on the mistaken belief that Stefanou had not filed *any* response at all. This was simply an oversight by the magistrate, as North River acknowledged in the district court; in fact, Stefanou filed a response asserting his Fifth Amendment privilege. On motion for reconsideration before the district court, North River sought to sustain the magistrate's ruling on the ground that Stefanou had waived his privilege by asserting it after the 15-day limit for discovery objections imposed by local rule. The district court refused to review the magistrate's

CONCLUSION

For the foregoing reasons, petitioner respectfully submits that the petition for writ of certiorari should be granted.

Respectfully submitted,

PETER J. KAHN
Counsel of Record

TERRENCE O'DONNELL
JOHN D. CLINE

WILLIAMS & CONNOLLY
839 17th Street, N.W.
Washington, D.C. 20006
(202) 331-5000

Attorneys for Petitioner
Peter Stefanou

April 21, 1988

---

ruling on the ground that it was moot, C.A. 197, and the court of appeals did not reach the issue.

North River's waiver claim provides no basis for denying the petition for certiorari. As the magistrate concluded in deciding another motion in this case, the local rule does not preclude assertions of privilege made after the 15-day limit. In any event, as Judge Hall noted in dissent in the court of appeals, the proper course would be a remand to the district court "to decide if Stefanou's response to the request for admissions was timely filed." App. 7a.